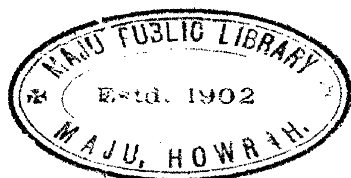
BANKS AND BANKING

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BANKS AND BANKING



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PREFACE.

This small volume consists of a series of notes on the growth and development of banking in this country. The author has endeavoured to show how the deposit of money in a bank has developed into a complex system of finance, and also how capital, wielding an immense power in the present day, is largely under the management and control of our great banking institutions. The study of banking is of great importance when we consider how dependent the commercial world is upon the existence of a perfectly sound system. To understand the why and wherefore of credit, which forms the basis of banking, is an essential study for those who have adopted it as their profession.

As to the sequence of the work it has been thought desirable, in the first place, to give a short sketch of early banking in this country, and then as an outcome of the expansion of trade to show its connection with commerce. In the early history of banking the subject of the currency was the most prominent feature, and therefore it has been treated separately.

The Bank of England occupies such an important position, that an account of the rise and progress of that institution is given. The subsequent chapters consist of a series of notes on the history of English, Scotch, and Irish Banks.

The connection between commercial crises and banking is of such an intimate character that the leading incidents of every important crisis have been given.

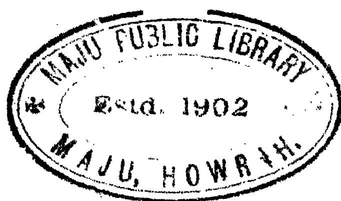
Modern banking is so dependent upon the rate of interest which determines the profits of banks that it has been considered desirable to give a somewhat lengthened account of the causes of fluctuations in the value of money.

The concluding chapters are devoted to incidents of modern practice, such as cheques, bills of exchange, and the opening of branch offices.

The author hopes that the notes may be of some value to those candidates who are preparing for the Institute of Bankers' Examinations.

Reference is made to such standard works as Bagehot's *Lombard Street*, Professor Jevons' *Money* and *Investigations of Currency and Finance*, Professor Marshall's *Principles of Economics*, and *Notes on Banking* by Mr. Palgrave, and the author trusts that his notes may serve as an introduction to such excellent manuals of finance. The yearly volumes of the Institute of Bankers have also been of great service, as they form almost an encyclopædia of banking.

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BANKS AND BANKING.

CHAPTER I.

INTRODUCTION.

THE study of banking is a subject of great interest, because the prosperity of this country is largely dependent upon the stability of our banking system.

We might almost say that the entire capital of the country finds its way into banks in order to be utilised for the benefit of the community. For example, a manufacturer by the aid of borrowed capital obtained from banks is able to produce commodities at a cheaper rate, and thus benefit society at large. It is a known axiom of political economy that an increase of production is a cheapening process. Our modern system of banking has materially increased the prosperity of this country, because no country in the world has the same financial facilities as we have for carrying on trade. Abolish our banking system, and we should find it difficult to compete with other countries; we should, in fact, be heavily handicapped.

Credit is the basis upon which our trade is transacted. One person takes a cheque from another because he believes the drawer has capital at his bankers, and that it will be paid on presentation. This system of credit is of comparatively recent origin, and it has been the means of economising the use of the precious metals. If the cheque system was abolished, a larger amount of gold would be required to act as a circulating medium.

Gold and silver must be bought like other commodities, and when stored in banks represent capital that is not required for the moment.

Our banking system is carried on with a very small amount of the precious metals, and therefore the capital of the country is economised. We should expect to find a country in a prosperous condition where a good system of banking exists.

English banking is comparatively modern. Two hundred and twenty years ago the English banker was a goldsmith, and also advanced money upon plate, jewellery, etc. The Bank of England was not in existence, the date of its charter being 27th July, 1694, and joint-stock banking in England was also unknown, although it was not declared illegal until the renewal of the Bank Charter in 1708.

At an earlier period the business of money lending was carried on by the Jews. They lent money at a very high rate of interest, although a law passed in the reign of Edward the Confessor prohibited usury.

However, we find that in the year 1199 the rate of interest was fixed by law at 10 per cent., and this appears to have been the rate until the reign of Henry VIII. It is stated that the Jews at Oxford during the reigns of Henry III. and Edward I. were in the habit of extracting 45 per cent. from the students. The matter was taken up by the legislature, and Henry III. granted a charter by which they were only to receive interest at the rate of 2d. in the £ weekly. Money so obtained from the Jews did not benefit the trade of the country, but only of individuals who were in pecuniary difficulties.

The Jews were thoroughly hated for the manner in which they transacted business, and consequently were expelled from England in the year 1290, and were not readmitted until the time of Oliver Cromwell.

The Lombards were also money lenders, and settled in this country at an early period from Genoa, Venice, Lucca, and Florence. They lent large sums of money to different governments, for which, like the Jews, they charged an exorbitant rate of interest. Edward III. borrowed 5000 marks from them, for which he paid 7000 marks.

Besides the Jews and Lombards there was another class who were originally dealers in gold and silver bullion, but who became subsequently bankers. These men were called goldsmiths, and possessed considerable wealth. Mr. Price in his *Handbook of London Bankers* gives a very interesting account of these early goldsmiths and money lenders.

Amongst the early goldsmiths we have Otto, in the reign of William I., and later Henry Fitz Alwin Fitz Leofstane, who was Lord Mayor of London for twenty-four years from 1189 to 1213. In the reign of Henry III. we meet with three goldsmiths, *viz.*, Thomas de Frowick, Warden of the Goldsmiths Company in 1270, and Alderman of Cheap Ward in 1279; William de Gloucester, Keeper of the Dies in 1255; and William, the King's Goldsmith, Master of the Mint in 1258. The names of seven goldsmiths are recorded between the years 1327 and 1377.

In 1566 the Court books of the Goldsmiths Company show that out of 107, no less than 76 of them resided in "Chepe"; the remaining 31 resided in "Lumberde Street". It was during the Commonwealth that the goldsmiths began to assume the character of bankers. Many persons left their money with the goldsmiths for safe keeping, and in return the goldsmiths gave receipts or cash notes for the same, payable on demand. These receipts passed from hand to hand, and were called goldsmiths' notes. At a later period the goldsmiths deposited their money with the Government.

There was a feeling of insecurity during the Civil War, and therefore money kept in large iron chests was removed to places of safety.

The chief investments for capital were land and cattle.

It is stated in the Verney memoirs that on the death of Lady Verney in 1641, she directs by her will that certain sums of money should be taken from her red box and distributed amongst her relatives.

During the same period we have several noblemen stating that their capital consisted principally of live stock on their estates.

Charles II., being in want of money, closed the Exchequer, and all payments to bankers who had deposited money in that place were suspended. The goldsmiths had at that time £1,328,526 on deposit, and the loss of this large sum naturally brought ruin upon them and their customers. It was not until five years after that the king caused *letters patent* to be granted to the goldsmiths covenanting to pay 6 per cent. per annum, but even this was discontinued in 1683.

The number of goldsmiths or bankers that were in existence at the end of the seventeenth century amounted to about 70 or 80, and at the end of another 100 years they had not increased. In the year 1801 there were 68 private bankers in London.

Many of the goldsmiths whose names we find recorded in the *Little London Directory* still exist as bankers of the present day. Of these we have Messrs. Hoare & Co., descended from James Hore or Hoare, a goldsmith keeping running cashes at the Golden Bottle in Cheapside, 1677; Messrs. Child & Co., descended from Messrs. Blanchard & Child of "Ye Marygold"; Messrs. Martin & Co., descended from Charles Duncombe and Richard Kent of "Ye Grasshopper," in Lombard Street; and Messrs.

Barnett & Co., descended from Humphry Stocks of the "Black Horse" in Lombard Street, but now amalgamated with Lloyds Bank.

The London bankers met with a serious rival in the year 1694, when the Bank of England was founded to carry on the business of banking. This institution three years later obtained the exclusive privilege of joint-stock banking. It was enacted "That during the continuance of the said corporation of the Governor and Company of the Bank of England, it shall not be lawful for any body politic or corporate whatsoever erected or to be erected (other than the said Governor and Company of the Bank of England), or for any other persons whatsoever united or to be united in covenant or partnership exceeding the number of six persons in that part of Great Britain called England, to borrow, owe, or take up any sum or sums of money on their bills or notes payable at demand, or at any less time than six months from the borrowing thereof".

Very little is known with respect to the country bankers. It is supposed that very few existed prior to the American War, but after the termination of that war they increased very rapidly. In the year 1797 there were 270 bankers carrying on business in the country. Unfortunately the country bankers did not possess the wealth of their London brethren. They issued notes, and at times did not have sufficient capital to pay them on demand.

It is stated that "multitudes of miserable shopkeepers in the country, grocers, tailors, drapers, started up like mushrooms and turned bankers. They issued notes and inundated the country with their miserable rags." Burke says that when he came to England in 1750 there were not 12 bankers out of London, but in 1793 there were nearly 400. This number was reduced by the crisis of

1797 to 270. Of the country bankers now in existence, the names of 61 appeared in the *Post Office London Directory* of 1803.

The London bankers ceased to issue notes at an early period, and found it advantageous to keep Bank of England notes as till money.

In reviewing this period of English banking we find that it made very little progress. The trade of the country was not sufficiently developed to require much capital. If it had increased very rapidly, perhaps the monopoly of joint-stock banking given to the Bank of England would have been removed at an earlier date. The profit of the bankers during this period was chiefly obtained by the issue of bank notes.

CHAPTER II.

BANKING AND COMMERCE.

BANKING is intimately connected with the trade of this country, and it is important to show that such is the case. If the trade of the country had not progressed, banking would not have attained its present position. The rapid growth of English trade during the present century is shown by the enormous increase in the imports and exports, in the revenue, and also by the great number of ships built to carry produce to and from this country.

The abolition of certain laws enabled the merchant to send his goods to foreign countries without paying excessive duties, and when this country adopted the principles of free trade a remarkable stimulus was given to British industries.

In the year 1820 the London merchants petitioned for free trade. Now, the function of trade is to supply other countries with goods which they require. When the trade of a country is limited, the economy of production is also limited; but when the interchange of commodities between different countries is allowed without any restrictions, then those countries will become prosperous. Each country is dependent upon another for commodities. One will devote its energies to one industry, say the production of corn; and another will manufacture machinery for the use of the corn-growing country. We also get a full division of labour, if countries are not restricted by laws which prevent it.

These are the best arguments in favour of free trade.

Free banking was also required, and consequently in the year 1826 it was enacted that joint-stock companies might be formed for the purposes of banking. Now, it is important to notice the want of more banking facilities consequent on the rapid growth of English commerce. The amendment of the laws relating to public companies, and known as the Limited Liability Acts, was the cause of the formation of a large number of companies for various purposes, although at the present time it is thought that certain alterations are required. Banking and insurance companies were not allowed to be formed on this principle until the year 1862, when it was enacted that any seven or more persons associated for *any lawful purpose* by subscribing a memorandum of association might constitute themselves a limited or unlimited company.

The abolition of the usury laws was another gain to banking and commerce. The Act of 1833 repealed the usury laws with regard to bills of exchange of three months and under. In the year 1837 this was extended to bills of twelve months and under, and in 1839 it was lawful to stipulate for any rate of interest upon which the parties might agree as to all personal contracts, but made an exception as to real securities. The usury laws were abolished entirely in the year 1854.

The tax on receipts was reduced to 1d. in 1853, and in 1854 the stamp duties on bills of exchange were reduced. The payment of custom duties by cheques, instead of by gold and notes, was of some importance to the bankers, because it lessened their gold requirements. We must always remember that the state of trade in this country is a question of vital importance to the banking institutions. The amount of capital held at the disposal of a banker will vary with the prosperity of the country. He

does not create capital, because his resources are obtained from those who deposit their capital with him. We might consider him as a broker between two principals: one deposits capital with him and he lends it to another whose solvency he guarantees. His position is, therefore, an important one, because he selects the borrower, and whether capital is utilised for a good purpose or sunk in unprofitable enterprises is dependent upon his ability to discern between a sound and an unsound borrower. The banker has also to discriminate between the mere speculator and the *bonâ fide* business man.

The rapid growth of trade required plenty of capital, and this could only be obtained through the medium of banks, which have become the great store-houses of capital. All the surplus money, say, of the agricultural districts, finds its way through the medium of banks into manufacturing districts where it can be utilised. When an industry is prosperous then bills of exchange representing transactions in that particular trade will be held by banks as security or otherwise. If the trade of any industry suddenly becomes bad, then there will be less bills representing it. Capital which has been utilised in that particular industry will find its way to some other trade in a more prosperous condition. The advantage of this large floating capital stored up in banks cannot be over-estimated, because without it we should not be in such a good position to compete with other nations or be able to carry on the production of commodities so extensively.

One of the chief reasons why our trade is so great is that there exists a great abundance of floating capital, which can be obtained from the bankers at a low rate of interest. We can easily see how the banker is dependent

upon the trade of the country for capital to carry on his business. If trade is bad, then there will be little accumulation of money in banks, but if good, then the capital in banks will be increased. Sometimes, however, the banks may have an accumulation of capital, but in consequence of depressed trade their is no demand for it.

Another important point to be noticed in connection with commerce and banking is the mode of carrying on business in the present day. We might say that modern trade is transacted by means of borrowed capital. A man of ability can, as a rule, obtain accommodation from his banker, who will discount his bills. Thus, the capital of a trader may only amount to £2000 or £3000, yet his transactions would be far in excess of that amount.

The trader carries on business in the present day either by obtaining advances on the goods bought or by discounting bills received for goods sold. The difference between cost of production and the interest paid to the banker would constitute his profit. This method of transacting business is, however, quite of recent origin, because years ago it was not deemed prudent to trade by means of borrowed capital.

The connection between the foreign trade of this country and banking has been considered by various committees of the House of Commons at different intervals, from 1800 to 1847.

The results of foreign trade are shown by the foreign exchanges or the settling of accounts between different nations. By this means the difference in value between the imports and exports is paid. There are also other payments to be made for public loans, investments, etc., to foreign countries. The excess or balance either for or against this country must be paid in gold, the only commodity which will settle international indebtedness.

CHAPTER III.

THE CURRENCY.

It has been considered desirable to give a separate account of the note issues of this country, because at the commencement of the present century banking profits were to a great extent dependent upon the amount of notes which a bank could issue.

The subject of the currency was also the most prominent feature in the history of banking until some time after the passing of the famous Act of 1844.

In the early history of banking many erroneous ideas were held in consequence of the question of the currency being interwoven with the former subject. It was thought at one time that the currency laws were really the cause of the commercial disasters which have occurred in this country at stated intervals. Now, it is quite clear that loss of capital is not in any way connected with the question of bank notes, but unfortunately these two questions have been mixed together in a very confused manner. No doubt many of the early bankers lent their notes to unsound borrowers, and by this means great disasters took place; but loss of capital was quite another matter.

At various times there has been too much capital converted from floating into fixed. We have already referred to floating capital as that which a banker lends to his customer. If, for example, capital is utilised in constructing a railway, we should call it fixed, because a great number of years would elapse before the capital was re-

produced. When this takes place no alteration in the currency laws can alter the condition of capital. Many early writers said: Give us more notes, and then all these panics, etc., will disappear; but the nation during periods of financial distress does not require more notes, but capital. It is therefore important to recognise that gold and bank notes are only mere machinery required for a certain purpose. If notes and gold were abolished, other means or *tools*, as Professor Price designates bank notes, would be found to carry on the interchange of commodities.

Prior to the passing of the Bank Act of 1844 bank notes had been at various periods below their par value. This was seen from the price of gold. In September, 1799, gold was £3 17s. 6d. per oz., but in June, 1800, the price of gold rose to £4 5s. per oz. Now this was due to the inconvertible bank notes in circulation.

The following table shows the depreciation:—

	Real value of bank note.
1st September, 1797, to 19th October, 1798	£1 0 0
13th April, 1804, to 15th October, 1805	0 19 6
9th October, 1810	0 18 4
12th February, 1811	0 16 11
26th March, 1811	0 16 3
25th October, 1811	0 15 11
2nd October, 1812	0 14 5
22nd January, 1813	0 15 0
6th August, 1813	0 14 2

Whenever there is a fall in the value of bank notes in comparison with gold, it shows that there is an excess of paper money in circulation.

The country bankers supported all kinds of wild speculation by lending these inconvertible notes, and when called upon to pay them they were unable to do so. In the panic of 1793, out of 400 country banks no less than 100 stopped payment, and the remaining 300 were much shaken.

During the years 1814-1817 eighty-nine country banks suspended payment, and in the year 1825 no less than seventy-three acted in the same manner. The country bankers could at this particular time discharge their liabilities by means of Bank of England notes, which were then at a discount, but were nevertheless a legal tender.

These great disasters called for some remedy. Many committees, both of the House of Lords and Commons, were appointed to inquire into the state of the currency. Most of the evils that had arisen were due to the suspension of cash payments by the Bank of England in the year 1797. The Bullion Committee of 1810 examined many witnesses in order to find out the cause of these disasters. One party stated that the bank notes were depreciated, and that the difference between the market price and the mint price of gold was the measure of the depreciation.

The other party asserted that the notes were not depreciated, but that the price of gold had risen. The Committee, however, came to the conclusion that the suspension of cash payments by the Bank of England *had caused the depreciation of the paper*, and that the sooner the Bank returned to paying its notes in gold the better it would be for the country.

It seems hardly credible that such a simple question should have been disputed. Whenever a note cannot be converted into gold on demand, it must depreciate in value. If the holder of an inconvertible note wishes to purchase goods, and tenders his note for payment, the seller might accept it, but only at a discount. Thus goods are valued at a higher price when notes are inconvertible. One of the disadvantages of an inconvertible paper currency is that it causes great fluctuations in prices. Bank notes in the present day are worth their

face value, because it is known that gold can be obtained in exchange for them.

The Restriction Act prevented the Bank from cashing its notes in gold, and was passed because the Government of the day were afraid that all the gold would leave the country. Thus, in the years preceding 1819, the Bank was frequently ready and anxious to pay in gold.

The evil results of this restriction, which was the cause of depreciated bank notes, were at last seen, and an Act of Parliament was passed making it compulsory on the part of the Bank of England and the country bankers to pay their notes on demand.

The Bank Restriction Act was continued absolutely from 5th July, 1819, to 1st February, 1820, when the Bank was permitted to pay notes in gold as follows, *viz.* :—

(1) Between 1st February and 1st October, 1820, the Bank was required to pay its notes in gold bullion of standard fineness at the rate of £4 1s. per oz., but only notes of the value or price of 60 ozs. of gold could be exchanged.

(2) Between 1st October, 1820, and 1st May, 1821, the Bank was required to pay its notes in gold bullion at the rate of £3 19s. 6d. per oz.

(3) Between 1st May, 1821, and 1st May, 1823, the Bank was to pay in gold bullion upon the same plan at the rate of £3 17s. 10½d. per oz., which was the Mint price of gold.

(4) From 1st May, 1823, the Bank was to pay its notes in the gold coin of the realm.

(5) Finally, all the laws which restrained the exportation of gold were abolished, and it was allowed to be exported or melted without incurring any liability.

The Bank of England commenced paying off its notes

under £5 in 1821, and the country bankers were allowed to issue notes under £5 until 1833. The Restriction Act mentions the price of gold as £3 17s. 10½d. per oz.

Now, as this concerns the metallic currency of the country, perhaps it will be more convenient to consider the relation of banking to this subject at once, before stating the still greater changes in the paper currency.

In the year 1816 it was enacted that gold alone should be the legal standard of value, and that silver should be the legal tender of value to the extent of 40s. only. From the reign of William I. to that of Henry III. we had in this country a silver currency. Gold coins were then gradually introduced as the wealth of the country increased. The value of the guinea was fixed at 21s. in the year 1717, but the sovereign took its place on 1st July, 1817.

The weight of the English sovereign is 123·27447 grains of English standard gold, there being 1 part of alloy to 11 parts of fine gold. From the weight of the sovereign we get the Mint price of gold, *viz.*, £3 17s. 10½d. per oz.

The Mint cannot issue a coin of less weight than 123·074 grains, or of a greater weight than 123·474 grains.

The quantity of gold which the nation ought to have in reserve to meet sudden demands is a question of considerable difficulty.

Bronze coin is only a legal tender for 1s.; country bank notes are not a legal tender.

The late Mr. Bagehot advocated the keeping of a large reserve of gold by the Bank of England. He showed that the Bank is now the only place where gold can be obtained in large quantities to meet any sudden demand. All the surplus gold coming into the country finds its way into the vaults of that institution, because the other bankers do not keep any appreciable reserve of the metal. The London bankers can always obtain gold

from the Bank of England, because they keep banking accounts with that institution.

The Bank of England is thus called upon to meet the requirements of the United Kingdom, and also to settle the differences of international trade. Whenever we experience a bad harvest there is generally a sudden drain of gold to pay for foreign corn to make up the deficiency of our harvest. All the spare money of the country bankers and of the Irish and Scotch banks is sent to London. This money is lodged with their London agents, who keep their cash reserves with the Bank of England, and consequently the latter institution becomes the final cash reserve of the country.

It has been stated that the bankers' balances at the Bank of England ought not to be utilised in the same manner as ordinary deposits by that institution, because of this system.

The following table shows the metallic reserve of the Bank of England from the year 1850:—

	£
1850	= 15,500,000
1855	= 11,000,000
1860	= 13,000,000
1865	= 14,000,000
1870	= 23,000,000
1872	= 24,000,000
1874	= 21,500,000
1875	= 22,000,000
1880	= 27,663,000
1885	= 24,173,000
1890	= 21,818,000
1895	= 35,645,000

Mr. Jevons stated in 1875 that the metallic circulation was as follows, *viz.* :—

Gold coin in circulation	= 100 millions.
Bullion in the Bank of England	= 15 ,,
Silver	= 15 ,,
Bronze	= 1⅛ ,,
	£131⅛ millions.

Although Mr. Bagehot insisted upon a large cash reserve, we must remember that the country only requires enough gold to interchange commodities, etc. If ever there exists a want for the circulating medium, it can, as a rule, be obtained by raising the rate of interest, and thereby attracting gold from abroad.

Another remedy may be found in a greater use of cheques for small amounts, temporarily, until we obtained our usual reserve of gold.

Sir John Lubbock has shown that gold is very little used in comparison with cheques. A sum of £19,000,000 paid into the Bank was made up as follows:—

Cheques and bills	£18,395,000
Notes	487,000
Coin	118,000
	£19,000,000

Thus the cash was only 3 per cent. and the coin only ½ per cent. of the total transactions.

If we compare the metallic circulation of the country with the note circulation, we find that the former has increased rapidly in comparison with the latter.

1819 note circulation, England and Wales	£40,000,000
1870 ,, ,,	30,000,000
Less	£10,000,000
1819 metallic circulation	£10,000,000
1870 ,,	105,000,000
More	£95,000,000

In the year 1844 the gold circulation was £36,000,000 and the note circulation £37,000,000, the notes therefore being slightly in excess.

The use of cheques has increased to an enormous extent in recent years: for example, in the year 1844 the Clearing House returns were equal to 40 times the note circulation, in the year 1872 the returns of the Clearing House were 135 times more. This tends to

show that a less amount of gold is now required in consequence of its being superseded by cheques, combined with other economical methods such as the use of telegraphic transfers. Again, the greater rapidity in the circulation of money tends to lessen the amount of coin required. We must always consider gold as a *tool* required to do certain work in the interchanging of goods. At present it is the best metal because of its great value, but if large quantities were found it would, like silver, depreciate in value. This depreciation might so increase that it would be the means of raising the value of other commodities measured by gold.

The country is not benefited by the import of large quantities of gold, unless required for the purpose of circulation. If there is a very large amount at the Bank of England, it shows that there is very little demand for capital.

Of course it is very important that the Bank of England notes should always be convertible into gold, and for this reason a fair reserve is necessary; but it must be remembered that the Bank has never been called upon to discharge its liabilities on *notes*, even at the most critical periods in the history of banking.

With these few remarks upon the gold currency we will now return to our former subject, *viz.*, the note circulation.

On the 19th June, 1828, an Act was passed which enabled bankers in England to issue certain unstamped promissory notes and bills of exchange upon payment of a composition in lieu of the Stamp duties thereon. The object of this Act was chiefly to give country bankers the same advantages in respect of drafts as were granted to the branches of the Bank of England. In the following month of the same year notes under £5 were forbidden under certain penalties. In the year 1832 a Committee

of the House of Commons discussed the question of the paper currency under the following sections:—

(1) Whether the paper circulation of the Metropolis should be confined to the issue of one bank, or whether there should be a competition of different banks of issue with an unlimited number of partners.

(2) Whether the note circulation of the country should be confined to one bank.

(3) What check should be provided to secure for the public a proper management of the banks of issue, and especially whether it would be expedient and safe to compel them periodically to publish their accounts.

The Committee did not draw up any report on these points, but from that time the Bank of England published a weekly statement of its accounts.

The crisis of 1836 brought the question of the currency again before the country. Lord Overstone stated that it was time the banking functions and the management of the currency should be separated.

In the year 1840 a Committee was again appointed to consider the effect of the paper currency on the country. Perhaps it will be as well to state the different opinions expressed upon this question prior to the passing of the famous Act of 1844.

Lord Overstone and Sir Robert Peel represented one party and Mr. Tooke and Mr. Fullarton the other.

Lord Overstone and Sir Robert Peel held:—

(1) That the amount of circulating medium may be greater or less than is properly required for the transaction of the current business of the community, and that where greater it tends by the excess to make the use of the circulating medium too cheap.

(2) As prices are measured by the circulating medium it enhances their price.

(3) That such enhancement, by reducing exports and stimulating imports, turns the foreign exchanges against us and leads to a drain of bullion.

(4) If the circulating medium be too low the opposite effect is produced in favourable exchanges and an influx of bullion.

(5) The principal cause of an undue expansion of the circulating medium is due to a too large amount of bank notes payable on demand.

(6) Issuers of notes can regulate at will the amount of them in circulation.

(7) If notes are kept in proper proportion to the bullion the amount of the circulating medium will be prevented from becoming greater than it should be, and the mischief held to arise will be avoided.

Mr. Tooke and Mr. Fullarton held:—

(1) That no greater amount of gold or notes is in circulation than is required by the current transactions of the country. If there is more it is hoarded up by the bankers.

(2) That while a large portion of the circulating medium is dependent solely upon the credit of its issuers, its extensions can in part only be limited by the state of that credit on one hand and by the aggregate demand of those who are willing to pay for its use on the other.

(3) That while there is a large fund of deposits in the banks issuing, a banker cannot affect the aggregate amount of circulating medium by issuing or withdrawing notes.

(4) A restriction of notes must be ineffectual, because bank notes only represent one portion of the addition made by the operation of bankers.

(5) That the true measure of the voluntary addition made by a banker is to be found in the terms upon which he makes his advances.

(6) That any attempt to control the issuing banker by law would be in fact an attempt to fix the price of the use of money.*

These different opinions show that the subject of the currency was not clearly understood.

After the passing of the Act of 1844, great disappointment was felt, because the great changes which it was supposed to accomplish did not take place.

No doubt the Act was good in some particulars. For example the convertibility of the note was secured, but commercial crises, panics, drains of gold, large issues of notes, and high rates of interest were as frequent after the year 1844 as they were previous to the passing of the Act.

The gradual extinction of the country bank issues was one of the objects intended by the framers of the Act, and it will be seen that the provincial circulation of notes has gradually diminished; but whether this was advisable or not is a question that has been much disputed.

The failure of many banks of issue was the chief reason why the Government by this Act intended to exercise some control over the note circulation. One of the popular errors with regard to paper money was that a banker could issue to an unlimited extent. Now the number of notes issued depends entirely upon the wants of the people. The banker cannot make his customers take notes, although he might be desirous of circulating a large number.

Again, the Bank of England cannot control its issue of notes, because any number can be obtained from that institution in exchange for gold. It was also supposed that notes could be issued by the Bank of England and that a certain amount of gold could always be held. Now this is impossible, because so long as notes are in circu-

lation, gold can be obtained for them on demand. It is therefore possible to drain the Bank of England of all the gold in its possession. We must remember that there is no creation of capital by a banker issuing notes, which only represent capital lent. Thus the holder of a note is really the lender of capital, although it appears that the banker acts in that capacity. In this manner the banker makes a profit on the capital entrusted to him through the medium of his notes.

It has been disputed whether the issue of £15,000,000 of notes by the Bank of England *against securities* is sufficient, but when that institution was allowed to issue to any amount without holding gold against the excess in the years 1847, 1857, and 1866, it was only in 1857 that an excess occurred, and then only for the comparatively small sum of £800,000.

Notes economise capital, because without them a larger amount of gold would be required for circulation. It is very important that they should be always convertible, and in order to secure this the Bank of England raises the rate of interest when the amount of gold held in reserve appears too small.

The Government, in consideration of the privileges given to the Bank of England in respect of the note circulation, receives in return £172,000 per annum, which is really a part of the Stamp duty.

With these remarks upon bank notes we will now consider the leading provisions of the famous Bank Act of 1844, upon which the currency of our country is now definitely settled.

CHAPTER IV.

BANK ACT OF 1844.

FROM and after 31st August the Issue Department of the Bank of England shall be separated from the Banking Department; that the Issuing Department may issue notes to the extent of £14,000,000 upon securities set apart for that purpose, of which the debt of £11,015,100 due from the Government to the Bank shall form a part; that no amount of notes above £14,000,000 shall be issued except against gold coin or gold or silver bullion, and that the silver bullion shall not exceed one quarter of the amount of gold coin or bullion.

Any person is entitled to demand notes from the Issuing Department in exchange for gold bullion at the rate of £3 17s. 9d. per oz.

Should any banker discontinue his issue of notes, the Bank of England may upon application be empowered by an Order of Council to increase its issue to the extent of two-thirds of the issue thus withdrawn, but all the profit of this increased issue must go to the Government.

The Bank of England is allowed to compound with issuing banks, and consequently forty-three banks in England made agreements to that effect with the Bank of England. The Bank of England is exempt from Stamp duty.

No new banks of issue shall be formed.

That bankers claiming to issue notes shall send a return of their issue during the twelve weeks next preceding the

27th April, 1844, in order to obtain the average amount of their issues.

Banks uniting need not give up their note issue, provided that it shall not be lawful for any such united bank to issue notes at any time after the number of partners therein shall exceed six persons.

Every banker must transmit a weekly account to the Commissioner of Stamps and Taxes.

Certain penalties are incurred by issuing more notes and not making returns in accordance with the Act.

The Bank of England's weekly account should be in the following form :—

ISSUING DEPARTMENT.

Notes issued.	Government debt.
	Other securities.
	Gold coin and bullion.
	Silver bullion.

BANKING DEPARTMENT.

Proprietors' capital.	Government securities.
Rest.	Other securities.
Public deposits.	Notes.
Other deposits.	Gold and silver coin.
Seven days' and other bills.	

In 1854 bank notes were defined by Act of Parliament as "bills, drafts or notes issued by a banker for the payment of money to bearer on demand, and which shall entitle the holder thereof without indorsation to the payment of any sum of money on demand, whether the same shall be expressed or not, in whatsoever form shall be deemed to be bank notes".

The following table shows the increase in the note circulation of the Bank of England :—

	£
1718 =	1,829,930
1778 =	7,030,680
1790 =	10,217,000
1800 =	15,450,000
1810 =	23,904,000
1819 =	25,657,610
1830 =	20,620,000

£
1840 = 17,231,000
1844 = 20,250,000
1850 = 19,520,000
1861 = 20,010,000
1865 = 21,090,000
1870 = 23,300,000
1872 = 25,540,000
875 = 27,346,000
880 = 26,915,000
1885 = 24,667,000
1890 = 24,961,000
1895 = 25,870,000

From these tables we observe that there has been a large increase in the note circulation of the Bank of England. This is more clearly seen if we compare the note circulation of the United Kingdom with the increase in the number of bank offices and also with the population.

Thus, while the population between 1851 and 1878 grew 23 per cent., the circulation of bank notes grew 35 per cent., and although the bank offices had increased 91 per cent., which would mean a greater use of cheques, there was still a great development in the note circulation.

The following table will show the present position of the issue of English country banks in 1896:—

	Private Banks.		Joint-stock.		Together.	
	No.	Auth. Issue.	No.	Auth. Issue.	No.	Auth. Issue.
By Act of 1844 . . .	207	£5,153,407	72	£3,495,446	279	£8,648,853
Since ceased to issue	145	£2,933,359	37	£1,521,244	182	£4,454,603
Amalgamated without loss of issue . . .	6				6	
	151				188	
Remaining . . .	56*	£2,220,048	35	£1,974,202	91	£4,194,250

* The recent amalgamation of private banks with Messrs. Barclay and Co. will reduce the number to 43, and the authorised issue will be £677,385 less

The following table shows the decrease in the average circulation of country banks since 1844 :—

	£
1844	=8,170,000
1850	=6,320,000
1855	=6,850,000
1861	=6,110,000
1865	=5,800,000
1870	=4,890,000
1875	=4,812,000
1880	=3,400,000
1885	=3,036,000
1890	=2,367,073
1895	=1,747,925

There has been a diminution of 43 per cent. in the issue of private banks and 55 per cent. in joint-stock banks. Of the issue of joint-stock banks, 74 per cent. was compulsorily forfeited under the Act and 26 per cent. by bankruptcy. Of the issue of private banks 32 per cent. was forfeited under the Act, 21 per cent. was given up voluntarily, and 47 per cent. was lost through bankruptcy.

Authorised issue lapsed :—

	£
1844-8	=423,410
1849-53	=282,981
1854-8	=234,174
1859-63	=173,212
1864-68	=753,814*
1869-73	=157,099
1874-75	=163,178
	£2,187,868
1875-95	=2,236,363
	£4,424,231

In consequence of the above lapsed issues the Bank of England authorised circulation has increased from £14,000,000 to £16,800,000.

* The large amount lapsed in 1864-68 was principally due to the National Provincial Bank giving up its issue on opening a London office.

From the above tables it will be seen that there has been a gradual diminution in the issues of country banks caused either by bankruptcy or amalgamation. Again the greater use of Bank of England notes has superseded the local issue.

The banks issuing notes within sixty-five miles of London have diminished in much greater proportion than those beyond, which is due to the fact of their nearness to London.

It is to be noticed that the country note circulation is less in August than in May, the difference being about £500,000.

Mr. Jevons has prepared a statement showing the variations from week to week from 1845 to 1862 :—

In 18th week of the year	£6,920,000
,, 31st ,, ,, ...	6,370,000
Diminution . .	£55,000
In 19th week of the year	£6,900,000
,, 32nd ,, ,, ...	6,350,000
Diminution . .	£55,000

Bank of England notes are a legal tender for payment of debts in England, but not in Scotland. With regard to country bank notes they are a legal tender if not objected to on that account, but the holder must circulate or present them for payment the next day after their receipt if he wishes to charge the transferor in case the banker fails. The holder, in fact, must treat country bank notes as cheques, in order to preserve his rights to sue in case of dishonour.

CHAPTER V.

NOTE CIRCULATION OF SCOTLAND.

THE note circulation of Scotland is peculiar to that of England because in the former country there is an issue of £1 notes. Thus in 1879, out of a total circulation of £5,522,000, no less than £1,974,000 represented £1 notes.

Another point to be noticed is the great confidence which the Scotch people have in their note circulation.

The issue of notes in Scotland is now regulated by the Act of 1845, but previous to that year any bank could be formed with the privilege of issuing notes.

The opposition to the Act of 1845 was overcome by giving the existing banks the sole right of issuing notes, which practically meant the exclusion of new banks in that country.

This Act imposed unequal conditions; for example, one bank was allowed to issue £1 for every £11 18s. 7d. of capital, whilst another could issue the same amount for £2 5s. 8d. of capital. Another hardship is supposed to exist in compelling the banks to keep gold in their vaults for the excess above the authorised issue.

There is always a large increase in the note circulation in May and November, consequent on the payment of rents, etc., being made on 15th May and 11th November. At these periods of the year large sums of gold are obtained from the Bank of England and sent down to Scotland in order that the Scotch banks can make their returns in accordance with the Act of 1845.

This hypothecated gold very soon finds its way back to the Bank of England after the returns are made up. The Scotch banks make a profit of about 2s. 6d. per cent. on their note circulation.

We will now state the leading provisions of the Act of 1845:—

(1) Scotch banks are allowed to retain their £1 notes.

(2) The power of issuing notes is confined to those banks that issued notes in the year preceding 1st May, 1845.

Banks amalgamating are allowed to retain the aggregate fixed issue of the separate banks. They may exceed their limits, but the excess must be represented by coin. They must make a return of the amount in circulation to the Stamp Office of the average amount of four weeks. If notes are in excess of the authorised circulation, and gold is not kept in reserve against such excess, then the bank which infringes the law must forfeit the amount not covered by gold.

Bank of England notes are not a legal tender in Scotland.

The Government reserves to itself the right of inspecting the books of the banks in order to ascertain the correctness of the returns.

The following tables show the present position of the note issue in Scotland:—

	Banks.	Fixed Issue.
By Act of 1845	19	£3,087,209
Reduction by Amalgamation . .	6	
Failure of Western Banks, including Ayrshire Bank . . .	2	337,938
	8	
Balance	11	£2,749,271
City of Glasgow	1	62,921
	10	£2,676,350

THE AVERAGE CIRCULATION SINCE 1844.

	£	Over limit of Act, 1845. £
1844	=3,020,000	210,000
1850	=3,220,000	140,000
1855	=4,100,000	1,020,000
1861	=4,200,000	1,450,000
1865	=4,380,000	1,630,000
1870	=5,110,000	2,360,000
1872	=5,320,000	2,570,000
1874	=5,904,000	3,227,650
1876	=6,099,000	2,227,650
1880	=5,550,000	2,873,650
1885	=5,745,000	3,068,650
1890	=6,276,323	3,599,973
1895	=6,938,879	4,262,529

The note circulation of Scotland has increased in far greater proportion than the population.

The English bankers complain that the Scotch banks have privileges which they do not possess. It would be impossible for any bank to succeed in Scotland unless allowed to issue notes and this is prevented by the Act of 1845.

It seems only just and right that the Scotch banks should forfeit their rights of issuing notes upon opening London offices. It is manifestly unfair that English country banks and Scotch banks should be treated differently. Of course it was never contemplated when the Act was passed that the Scotch banks would open London offices.

CHAPTER VI.

NOTE CIRCULATION OF IRELAND.

THE note circulation of Ireland was finally settled by the Act of 1845. The authorised issue, like that of the Banks of Scotland, was to be the average amount of the year ending 1st May, 1845. If any two banks amalgamate the new institution may issue to the amount of the circulation of the united banks. If any bank voluntarily surrenders its right to issue, and agrees to issue Bank of Ireland notes, the Bank of Ireland may increase its authorised issue to the full amount of the issue of the bank which has surrendered its right of issue. This provision is quite different from the Act relating to Scotland.

In Ireland all notes must be payable at the place or places where they have been issued or reissued, whilst in Scotland notes issued at the branch office are payable only at the head office. The amount of gold held for the excess of the authorised issue in Ireland must be held at the chief office, or at four chief places of issue.

No new bank of issue can be formed. The issue of notes in Ireland was in private hands until the establishment of the Bank of Ireland in 1782 with a monopoly of banking, but an Act passed in 1821 allowed joint-stock banks to issue notes, provided they had no office in Dublin, or sixty-five miles beyond.

When the Act of 1845 was passed no private bank issued notes in Ireland.

The following table shows the increase in the note circulation of Ireland since 1844:—

AVERAGE CIRCULATION.

	£	limit of Act, 1849. Above or under £
1844	=5,940,000	+ 600,000
1850	=4,510,000	- 1,840,000
1855	=6,360,000	+ 10,000
1861	=6,260,000	- 90,000
1865	=5,980,000	- 370,000
1870	=6,880,000	+ 330,000
1875	=7,064,000	+ 710,000
1880	=6,548,000	+ 194,000
1885	=6,225,000	- 139,494
1890	=6,838,716	+ 474,222
1895	=6,400,123	+ 45,629

The eight banks which issued notes were reduced to six by amalgamation, but the fixed issue remained the same, *viz.*, £6,354,494.

The effect of the bad harvests in Ireland and also the social and political disturbances in that country is exemplified by the note circulation in recent years. Thus, comparing 1879 with 1878 there has been a fall of 13 per cent. If we compare the laws which regulate the English country note circulation with that regulating the Irish and Scotch circulation, we observe that £1 notes are only allowed to be issued in Scotland and Ireland. Again, Bank of England notes are not a legal tender for money either in Scotland or Ireland.

The English banks cannot exceed the limit fixed by the Act of 1845, whilst the Irish and Scotch banks can do so if they keep the excess of such issue in gold. The English banks make a return of their weekly amounts, whilst the Scotch and Irish banks return only a monthly amount of their notes in circulation.

In England, when two banks amalgamate, their right of issuing notes is forfeited. The following table shows the average note circulation of the banks in the United Kingdom :—

BANKS OF ISSUE IN 1874.

	Lowest Actual Circ. per Bank.	Highest Actual Circ. per Bank.	Average Actual Circ. per Bank.
England and Wales—			
Private Banks .	£1,825	£125,937	£23,000
Joint-stock Banks	1,191	311,641	43,700
Scotland . . .	104,000	789,000	536,300
Ireland	476,000	2,879,000	1,128,200

The Banking Act passed in 1879 allows the English joint-stock banks to protect their note issue by stating in the articles of association that the term limited liability does not apply to the note issue, and that shareholders will continue liable in respect of notes issued in the same manner as an unlimited company.

CHAPTER VII.

BANK OF ENGLAND.

THE foundation of the Bank of England is due to William Paterson, a Scotchman, who in 1693 proposed that the expenses of the war with France should be met by a national loan. Forty merchants subscribed £500,000 towards the sum of £1,200,000 lent to the Government at the rate of 8 per cent. per annum. For this consideration, the subscribers were to be made a corporation under the title of the Governor and Company of the Bank of England.

The Act passed in 1693 stated: "Their Majesties may make commissioners take subscriptions for £1,200,000"; and section 20 states: "Their Majesties may appoint rules for transferring, and make the subscribers a corporation by the name of the Governor and Company of the Bank of England".

The Bank of England did not originally have the sole monopoly of joint-stock banking, but when it was proposed to start another bank in 1708 on the same principles, the directors succeeded in obtaining that monopoly.

The Charter was renewed in 1697, 1708, 1713, 1716, 1721, 1742, 1746, 1749, 1764, 1781, 1800, 1808, 1816, 1833, and 1844.

Mr. Bagehot considered the monopoly given to the Bank of England was injurious for the following reasons, *viz.*:—

(1) Banking ought to be free, because monopolies are likely to be injurious to the public unless kept within reasonable limits.

(2) The Bank, being in some indirect manner connected with the Government, is supposed by many to be in reality a Government institution.

(3) By this means it had a better reputation than other institutions of a like character.

(4) When crises, panics, etc., occur in the country, it was expected to lend money to all comers.

(5) Finally, in consequence of this monopoly, it became the sole cash reserve for the country.

No doubt the Bank occupied a far more important position than it does at the present time. The rapid growth of English joint-stock banks has been the cause of this change.

The Bank of England is managed by a governor, a sub-governor, and twenty-four directors. The late Mr. Bagehot thought it would be better if the Bank had a permanent head rather than a continual change of governors. The re-election of Right Hon. W. Lidderdale during the Baring crisis shows somewhat the necessity of having a permanent governor. The Bank of France has a permanent head, the governor being appointed by the Government for life.

The influence and position of the Bank of England during the eighteenth century were far greater than in the present day. The London bankers were then very jealous of its position. Its large capital and its large issue of notes made it a very formidable opponent.

We can easily understand how it came to pass that the Bank should fix the rate of interest for money. Being the only joint-stock bank, and also holding large deposits in comparison with the private bankers, caused it to assume that position.

We have stated that the rate of interest fixed by the Bank of England became the market rate, but the enor-

mous increase of capital in the other banks has now led to an alteration in this respect.

The London joint-stockbanks have in a certain degree abandoned their usual plan of allowing interest on deposits to be governed by the Bank rate.

The Bank of England is comparatively a small lender of money and therefore its rate does not indicate the real value of money in the market. We must ascertain exactly the *whole* supply of capital and demand for it before we can ascertain the correct rate of interest. Including loans and discounts the Bank lends less than $\frac{1}{6}$ of the amount lent by the London joint-stock banks and less than $\frac{1}{5}$ of that lent by the London Bill brokers.

However, as a lender of money, it has always exercised great caution, and only advanced money upon the best securities. The capital of the Bank amounts to £14,553,000, which is enormous compared with the capital of other banks, and tends to keep the dividends low. Thus from 1797 to 1822 the dividends were from 10 per cent., and from 1817 to 1876 the average was 8·6 per cent.

The Bank was started on condition that a certain sum, *viz.*, £1,200,000, should be lent to the Government. The increase in the following years was due to further loans to the Government of the day, and in return it obtained renewals of its charter and also other advantages.

The following table shows when loans were made to the Government and the balance of debt still due to the Bank of England:—

	£
1694=	1,200,000
1708=	2,175,000
1716=	4,175,000
1721=	9,100,000
1742=	10,700,000
1746=	11,681,000
1816=	14,686,000
1844-76=	11,015,000

The following table shows the increase in its liabilities:—

	£
1797	= 13,770,390
1833	= 30,937,000 (including notes)
1844	= 14,550,000
1850	= 18,800,000
1855	= 17,800,000
1865	= 21,200,000
1872	= 29,300,000
1885-91	= 32,630,000
1895	= 46,000,000

Since the passing of the Bank Act of 1844 its reserve from 1846 to 1891 in proportion to its liabilities has diminished—

from 1846-54 = 51 per cent.
,, 1864-72 = 42 ,, ,,
,, 1885-91 = 42 ,, ,,

but in 1895 the proportion increased to 58 per cent.

In this country the Bank of England is the only bank where large amounts of gold can be obtained to meet home and foreign demands, etc. Its position therefore as a bank of discount is very often impeded, because the rate of interest is advanced in order to prevent the reserve of gold getting too low.

It has been mentioned that the Bank Act of 1844 divided the issue from the banking department, and from that time the two offices were kept separate.

The weekly returns were to be drawn up as follows:—

Issue Department.

Notes issued.	Government debt.
	Other securities.
	Gold coin and bullion.
	Silver bullion.

Banking Department.

Proprietors' capital.	Government securities.
Rest.	Other securities.
Public deposits.	Notes.
Other deposits	Gold and silver coin.
Seven day and other bills.	

The business of the Bank of England consists of three groups or divisions, *viz.*: (1) The management of the National Debt. (2) Issue of bank notes. (3) Government and private banking.

The Government pays the Bank about £172,000 per annum for undertaking the entire management of the National Debt. This debt amounts to £589,147,000, and is divided amongst about 170,000 holders.

Although no interest is allowed the deposits in recent years have increased to a large extent, showing the confidence which the public have in that institution.

ANNUAL AVERAGE OF DEPOSITS.

	£
1844	= 13,300,000
1850	= 17,600,000
1855	= 16,800,000
1860	= 20,100,000
1865	= 20,700,000
1872	= 29,300,000
1875	= 26,413,000
1880	= 32,950,000
1885	= 33,451,000
1890	= 33,364,000
1895	= 40,556,000

Whenever there has existed in the country a feeling of distrust against banks, leading to a withdrawal of deposits, the Bank of England has always been an exception. The deposits during such periods have invariably increased. We might consider it as a model institution for the other banks of the country.

If at any time its management has been censured, it was in consequence of its position as a bank of issue, or as a bank holding the gold reserve of the country. It cannot be said that the Bank has lent money in a reckless manner.

The public deposits vary considerably according to the requirements of the Government. It has been stated

that it would be better for the Money Market if the Government account was divided amongst the various banks of the Metropolis, on the understanding that such banks should hold Government securities against the Government balances. This would have prevented large withdrawals of available capital from one institution instead of from a larger number. Every bank in this case would keep a certain reserve against the said balances.

The seven day and other bills issued have diminished considerably. In the year 1844 they were more than £1,000,000, now they only amount to £201,000. The great decrease in these bills is no doubt due to the greater facilities offered by the joint-stock banks of the country. All the branch banks issue drafts upon their London offices.

The "other deposits" stated in the weekly report include the bankers' balances, which certainly ought to be utilised by the Bank with great caution.

Mr. Hankey states that when the bankers' balances are very large, the Bank does not use the amount in excess. These balances form a part of the reserve of the bankers and the amount has increased considerably in late years. If the London bankers kept their own reserves, they would collectively keep a larger amount. At times we may expect to see fluctuations in the rate due to the Bank holding the cash reserves of other banks.

We will now consider the assets in the Banking Department.

The Government securities amount to £10,785,000; thus nearly the whole of the capital of the Bank is invested in interest-bearing securities.

The amount of the other securities has increased as follows:—

	£
1844 =	9,400,000
1850 =	11,100,000
1855 =	15,300,000
1865 =	20,500,000
1870 =	18,600,000
1872 =	21,400,000
1892 =	29,777,000

These other securities include the bills discounted. If we deduct the temporary advances and the bills discounted we find that the fluctuations of the remainder have been small in late years:—

	£
1844 =	5,400,000
1850 =	7,200,000
1860 =	11,100,000
1870 =	8,500,000
1872 =	10,600,000

The bills discounted from 1844 to 1872 have fluctuated greatly, which is due to the fact that any one properly introduced may have a discount account. This is quite a different method from that of the other London banks. However, the Bank as a discounter of bills does not occupy in the present day the same position as in former years. This is in consequence of the growth of capital leading to the formation of joint-stock banks and discount companies.

The competition between the Bank and the outer market is great. If the Bank's rate is below that of the outer market, there will be a large increase of business from outsiders. This would cause a demand, and consequently the rate of interest rises.

In consequence of competition in recent years, the Bank stated that although the published rate was the official minimum, yet under certain conditions it would discount bills at a lower rate of interest.

During commercial crises the bills discounted amount to a very large sum, because every one expects at such

times it should lend money in the shape of loans and advances.

Mr. Hankey states that the Bank ought never to have encouraged this opinion, but at these periods it has been found expedient to lend freely. In the year 1825 the directors stated: "The Bank had taken a firm and deliberate resolution to make common cause with the country".

Its position during the commercial crises of 1847, 1857 and 1866 was entirely due to monopoly. If banking had been free, the risks would have been divided amongst many banking institutions, and consequently tend to minimise panics.

At the present time the joint-stock banks have larger reserves, and therefore would not be so dependent upon the Bank of England in cases of emergency.

The following table shows the average amount of bills discounted:—

	£
1834	= 1,800,000
1844	= 2,700,000
1855	= 6,000,000
1866	= 9,600,000
1868	= 5,000,000
1872	= 6,900,000
1873	= 7,737,000
1874	= 4,665,000
1875	= 4,402,000

The average rates of discount have decreased in recent years.

Average rate from 1844-1856 = £3 15s. 3d. per cent.
" " 1857-1872 = £4 3s. per cent.
" " 1890-1894 = £3 1s. 10d. per cent.

The latter half of the year always shows the highest rates. This is in consequence of more business being transacted in autumn and early spring.

Average Rates of Discount.

1844	= $2\frac{1}{2}$ per cent.
1850	= $2\frac{1}{2}$ per cent.
1855	= $4\frac{3}{4}$ per cent.
1860	= $4\frac{1}{4}$ per cent.
1865	= $4\frac{3}{4}$ per cent.
1870	= 3 per cent.

Correct Rates.

	£	s.	d.
1875 =	3	4	8
1876 =	2	12	1
1877 =	2	18	0
1878 =	3	15	8
1879 =	2	10	4
1885 =	2	17	7
1891 =	3	5	2
1892 =	2	10	7
1893 =	3	1	0
1894 =	2	2	3
1895 =	2	0	0

Average Rates.

	£	s.	d.
1825-44 =	3	11	10
1845-91 =	3	14	6
1845-74 =	3	18	5
1875-91 =	3	5	9
1885-94 =	3	3	2
1844-79 =	3	16	3
1885-91 =	3	8	4
1890-94 =	3	1	10

The action of the Bank during commercial crises we shall consider separately. Since the year 1825 the following facilities with others have been granted to the customers of the Bank :—

(1) The Bank receives dividends by power of attorney for all persons having drawing accounts at the Bank.

(2) Cheques may be drawn for £5 and upwards instead of £10 as heretofore.

(3) Cash boxes taken in, contents unknown, for such parties as keep accounts at the Bank.

(4) Bank notes are paid at the counter instead of drawing tickets for them as heretofore.

(5) Cheques on city bankers, paid in by 3 P.M., are received and passed to account the same evening.

(6) Bills of exchange payable at the Bank are paid with or without advice, heretofore with advice only.

(7) Notes of country bankers payable in London are sent out the same day for payment.

(8) Cheques are given out in books and not in sheets as heretofore.

CHAPTER VIII.

JOINT-STOCK BANKING.

One of the reasons why joint-stock banks were allowed to be formed in this country was in consequence of the failure of many private bankers. Thus in 1793 one hundred stopped payment, the same number in 1810, a greater number in 1812, and in 1814, 1815 and 1816 about 360, making a total of nearly 1000 from 1791 to 1818. However, the first joint-stock banks formed were not more successful than their rivals. Again it was thought that banking was a very profitable business.

It was also discovered that the Bank of England's Charter stated "only borrowing or owing money on their bills or notes" was prevented, and therefore it was quite possible for a joint-stock bank to be formed to receive money on deposit.

Mr. Joplin stated in 1823: "That public banks have not hitherto existed, more especially in London and Lancashire, seems to have risen from the want of a proper knowledge of the principle of banking rather than from the Charter of the Bank of England, *which I find does not prevent public banks for the deposit of capital* from being established".

An attempt was made to induce the Bank of England to give up its monopoly of exclusive banking, but that institution would not, however, agree to the proposition. The Government, nevertheless, in 1826 passed an Act allowing joint-stock banks to be formed beyond sixty-five miles of London.

The statute states: (1) "That banks of an unlimited number of partners may be formed, provided that they shall not have any house of business in London or at any place within sixty-five miles thereof.

(2) "No such banking company was to issue or reissue either directly or indirectly within the prescribed distance any bill or note payable to bearer on demand or any bank post bill, nor draw upon its London agents any bill of exchange payable on demand, or for any less sum than £50, but they might draw any bill for any sum of £50 and upwards in London or elsewhere at any period after date or after sight.

(3) "Banks of an unlimited number of partners may issue notes, but they must deliver at the Stamp Office an account containing the names of the firm, etc.

(4) "Co-partnerships may sue or be sued in the names of their public officers.

(5) "The Governor and Company of the Bank of England may empower agents to carry on banking business at any place in England."

Banks were very soon formed in various parts of the country; thus in 1826 there were joint-stock establishments at—

Liverpool.
Manchester, and two branches.
Manchester and Liverpool, } and nine branches.
Birmingham.
Wolverhampton.
Sheffield.
Barnsley.
Bradford.
Halifax.
Huddersfield.
Knaresboro'.
York.
Darlington.
Lancaster, and three branches.
Whitehaven.
Carlisle, and seven branches.
Leicester.
Norwich, and nine branches.
Stamford.
Spalding.
Gloucester.
Langport, and fourteen branches.
Plymouth.
Devonport.

Unfortunately the supply of joint-stock banks was far

greater than the demand. A few years later a large number of them failed through lending money in a reckless manner.

People began to look upon them with distrust. Lord Overstone observed in 1832: "I think the joint-stock banks are deficient in everything requisite for the conduct of banking business except extended responsibility. The banking business requires peculiarly persons attentive to all its details, constantly, daily, hourly watchful of every transaction, much more than mercantile or trading business. Joint-stock banking, of course, obliges to act through agents and not by a principal, and therefore under the restraint of general rules cannot be guided by so nice a reference to degrees of difference in the character of responsibility of parties, nor can they undertake to regulate the assistance to be granted to concerns under temporary embarrassments by so accurate a reference to the circumstances favourable or unfavourable of each case."

These remarks of Lord Overstone were no doubt quite correct with reference to loans on personal security, but when banks were formed in London it was impossible to carry on business on these principles, consequent on the rapid development of trade in the Metropolis. A London banker cannot study and know the position and standing of each individual to the same extent as the country banker.

In the year 1833 banks were allowed to issue notes above £50 payable on demand in London. They were required by this Act to keep a weekly account of their notes in circulation and make a return to the Commissioner of Stamps. On the renewal of the Charter of the Bank of England in 1833, the Government would not alter it, so as to prevent joint-stock banks being formed in

London. They therefore inserted a clause allowing joint-stock banks in London provided they did not borrow or take up in England any sum or sums of money on their bills or notes payable on demand or at any less time than six months from the borrowing thereof. No partnership that exceeds six persons shall make or issue in London or within sixty-five miles thereof any bill of exchange or promissory note or engagement for the payment of money on demand or upon which any person holding the same may obtain payment on demand.

This Act also stated that an account of the bullion, notes in circulation and deposits in the Bank of England shall be transmitted weekly to the Chancellor of the Exchequer. Joint-stock banks were soon formed in London after the passing of this Act. The London and Westminster began business in 1836, the Union Bank in 1839, the London and County in 1839, and the Commercial Bank of London in 1840.

The London and Westminster Bank in its prospectus stated that it would receive current accounts on the same terms as other London bankers. No interest would be allowed on any current account. Deposit receipts would be issued for sums from £10 to £1000 bearing interest at the rate of 2 per cent. per annum, but if the amount should be withdrawn within three months, no interest would be allowed. Parties respectably introduced not having an account at the bank might nevertheless have their bills discounted or loans granted them on approved securities. The bank would act as agent to joint-stock banks, private bankers, and other parties residing at a distance. Persons who should require letters of credit to any part of the United Kingdom, the Continent of Europe, or other parts of the world, might obtain them.

The joint-stock banks formed in London had to contend with great difficulties. These banks existed only in the form of an ordinary common law partnership and consequently in an action all the shareholders had to join. This was not remedied until the year 1844. The London and Westminster Bank applied for a bill to sue and be sued in the name of its chairman, but this was refused. In consequence of this all the London joint-stock banks were sued in the names of trustees.

The Bank of England refused to open accounts for the new banks in its books and the private bankers would not admit them to the Clearing House.

The Act which permitted their formation did not allow them to accept bills at a less date than six months. In the year 1838 an Act was passed which allowed "a banking company to sue and be sued by any of its members exactly as if they were separate individuals". Prior to the passing of this Act, a shareholder in two different banks was unable to take proceedings. In the year 1840 this was extended to criminal cases.

By an Act passed in 1856 retiring directors in banking companies were made eligible for re-election.

In the year 1857 joint-stock banks were bound to register themselves in the same manner as other companies. This Act also allowed the number of partners in private banks to be increased to ten. Banks were allowed to be formed with limited liability in the year 1858, and all those that were formed after that date were on this principle.

This was beneficial, because shareholders as a rule like to know the extent of their liability. If a bank is unlimited there is a tendency for its shareholders to consist of a class with little capital. It has been suggested that directors of banks should be liable to an unlimited extent

in order to give a greater protection to shareholders, but we think there would be some difficulty in obtaining directors of high repute if such conditions were imposed. If a bank is registered as a limited liability company, it is still desirable that it should have a portion of its capital uncalled, as a protection to its depositors.

The following table will show the various dates at which the joint-stock banks were formed in this country :—

From 1826	to	1830	= 10
1831	,,	1835	= 28
1836	,,	1840	= 34
1841	,,	1845	= 3
1846	,,	1850	= 0
1851	,,	1855	= 1
1856	,,	1860	= 0
1861	,,	1865	= 26
1866	,,	1870	= 5
1871	,,	1874	= 11
			118

These banks are divided as follows :—

	1845.	1860.	1865.	1870.	1875.	1895.
Purely London Banks . .	4	7	11	12	12	5
London and Provincial Banks	1	2	9	8	7	12
Provincial Banks	—	85	93	92	99	82
	5	94	113	112	118	99

Some of these banks have a large number of branches. The number of bank offices has largely increased in recent years.

In 1851 = 962	offices =	1	office to	18,700	inhabitants.
1854 = —	,,	1	,,	16,500	,,
1870 = 1651	,,	1	,,	13,500	,,
1875 = 1885	,,	1	,,	12,600	,,
1878 = 2195	,,	—	,,	—	—
1883 = 2381	,,	1	,,	11,135	,,

In the year 1877 no less than seventy-five new bank offices were added in England and Wales.

The following table shows the increase in joint-stock banks from 1844 to 1894:—

	1844.	1894.
Joint-stock Banks, head offices	106	99
Do. do. branches	498 = 604	2577 = 2676

These tables show the enormous growth of joint-stock banks in this country.

Mr. Gilbart stated that the capital of a bank should be at least one-third of its liabilities, but when we see banks paying large dividends, from 15 per cent. to 20 per cent. and upwards, we may be sure that the capital is small in proportion to their liabilities. In Scotland the proportion is about one-sixth, but the London banks show a much smaller proportion.

In the year 1876 there were 116 banks, with the enormous capital of £31,151,429. These banks have accumulated out of their profits as reserve, the sum of £12,973,218. Thus:—

	No.	Capital.	Reserve.
Purely London Banks . .	12	£7,364,472	£2,138,844
London and Provincial Banks .	7	4,424,964	1,684,138
Purely Provincial Banks . .	97	19,361,993	9,150,236
	116	£31,151,429	£12,973,218

The increase in the banking capital of the United Kingdom in 1876 was £1,908,291, in 1877 £1,800,000, and in 1878 £1,200,000. In the year 1876 there was an increase in the capital and reserve of ninety-three banks, in 1877 of ninety-five banks, and in 1878 of eighty-four banks.

This is very satisfactory, because it shows that the banks are strengthening their reserves against increasing liabilities. In the year 1878 fully £1,000,000 of capital was lost by the failures of the City of Glasgow and West of England Banks.

The prospectus of the London and Westminster Bank, which we have quoted, stated that money would be taken on deposit. Although this is the usual practice amongst bankers, yet it has been stated that it is no part of a banker's business to find investments for those who are not customers, but who wish to leave money at interest.

The competition between bankers, bill brokers, and foreign and colonial banks in London has made it difficult to employ deposit money at a profit.

If money "at call" is ½ per cent., and first-class paper is discounted at ¾ per cent., it is a question whether bankers can afford to pay even ½ per cent. on deposits. It was stated recently in a London paper that when call money was ¼ per cent. it scarcely paid for the ink, paper and labour in making the necessary entries. We must not forget to include the working expenses before ascertaining the amount of interest which a banker can pay on deposits.

In times of distrust the depositor is generally the first one to demand his money, and therefore it is a question whether bankers ought to encourage deposit banking. The recent Australian banking crisis shows that the depositors are the first to take alarm; in fact the banker might consider the depositor as his natural enemy.

The growth of deposits and current accounts in some of the London banks is shown in the following table:—

	1844.	1874.
London and Westminster . .	£2,697,000	£30,020,000
Joint	2,245,000	16,000,000
Union	1,591,000	14,120,000
Commercial Bank of London . .	240,000	———
London and County	1,231,000	20,072,000
City	———	3,290,000
Imperial	———	2,100,000
Central	———	770,000
Alliance	———	1,922,000
Metropolitan	———	390,000

or an increase of 10·10 per cent.

The deposits of the London and Westminster Bank increased from £266,844 in the year 1835 to £1,361,545 in the year 1840.

The following table shows the increase in the deposits, etc., of the principal joint-stock banks in London from 1849 to 1859:—

Where Formed.	Capital. £	Bank.	Year.	Current and Deposit Accounts. £	Increase Per Cent.	Guarantee and Reserve Fund. £	Proportion of Capital & Guarantee to Deposits.	Dividends and Bonus. Per Cent.
1834	1,000,000	London	1849	3,680,000		108,000		6
		and	1854	7,177,000	95	134,000	16	14
		Westmr.	1859	11,115,000	55	200,000	10	18
1836	600,000	Joint	1849	2,792,000		132,000		9¾
			1854	6,161,000	120	156,000	12	25
			1859	9,556,000	55	229,000	9	18
1839	720,000	Union	1849	2,835,000		50,000		6
			1854	7,031,000	148	50,000	11	15
			1859	9,318,000	33	95,000	9	15
1839	500,000	London	1849	1,675,000		28,000		6
		and	1854	3,779,000	126	62,000	15	12
		County	1859	4,975,000	32	105,000	12	11
1855	300,000	City Bk.	1859	2,223,000		33,000	15	6

The London and Westminster Bank, for example, increased its amount on current and deposit accounts in ten years from £3,000,000 to £11,000,000, and the London Joint-stock Bank from £2,700,000 to £9,500,000.

The deposits in the London joint-stock banks sometimes show a decrease during a period of distrust. This is shown by the following table in 1878, when there were several bank failures:—

	Cash Deposits.		
	Dec. 31, 1878. £	June 30, 1878. £	June 30, 1871. £
London and Westminster	21,490,000	26,760,000	22,770,000
Joint	13,850,000	14,680,000	14,610,000
Union	12,400,000	12,540,000	12,710,000
City	2,870,000	3,920,000	2,360,000
Alliance	1,810,000	2,430,000	1,600,000
Carry Forward .	52,420,000	60,330,000	54,050,000

	Cash Deposits.		
	Dec. 31, 1878.	June 30, 1878.	June 30, 1871.
	£	£	£
Brought Forward	52,420,000	60,330,000	54,050,000
Imperial	1,620,000	2,270,000	2,230,000
Consolidated	2,560,000	2,960,000	2,450,000
Central	960,000	1,140,000	570,000
Metropolitan	—	320,000	590,000
London & South Western	1,560,000	1,570,000	570,000
Totals	59,120,000	68,590,000	59,860,000

The paid-up capital and reserve of these London banks amounted to £10,370,000 on 31st December, 1878, and £10,490,000 on 30th June, 1878.

The *Economist* gives the final results of totals and averages of the entire London banks for the period 1875-1878, as follows:—

I.	1878.	1877.	1876.	1875.
Capital paid up and reserves	£ 10,530,000	£ 10,370,000	£ 10,270,060	£ 10,090,000
II.				
Cash deposits	59,440,000	68,720,000	71,420,000	74,690,000
III.				
Business profits	1,210,800	1,133,500	1,061,000	1,285,000
Equal on cash deposits, per cent.	37s. 10d.	32s. 10d.	29s. 4d.	33s. 7d.
IV.				
Expenses	461,990	447,450	435,000	415,000
Equal on cash deposits, per cent.	14s. 6d.	13s. 5d.	11s.	10s. 11d.

Cash Deposits, 31st December, 1894.

	£
London and Westminster	26,386,000
Joint (including Imperial)	14,444,000
Union	14,120,000
City	6,647,000
Parrs and Alliance	13,179,000
Consolidated	3,421,000
London and Midland (formerly Central)	12,167,000
London and South Western	6,510,000

There has been a gradual decline of net profits in recent years. Thus the purely Metropolitan banks, *viz.*, London and Westminster, Union, Joint-stock, City, London and

South Western, Consolidated, and Martins, show a net profit of 8s. 6d. per cent., whereas twenty years ago it was 22s. per cent.

Unfortunately it is impossible to give the same details showing the progress of the joint-stock country banks, because a large number of them did not publish balance sheets until quite recently, but in order to show the rapid progress of English banking, we give the following statement of 100 banks, *viz.* :—

100 BANKS, ENGLAND AND WALES.

1883.	Deposits	£286,100,000
	Cash and money at call	79,550,000
1895.	Deposits	485,277,000
	Cash and money at call	144,163,000

Comparing 1869 with 1878 we find that the banks paying between 5 per cent. and 10 per cent. were more in 1869 than at the present time. The profits have increased with the greater activity in trade, and it is satisfactory to note that the reserves have increased more than the profits.

Total of reserves	1869 =	£12,815,000
	1878 =	21,297,000

or an increase of 60 per cent. for 110 banks :—

	1869.		1878.	
	No.	Capital.	No.	Capital.
		£		£
Banks paying 20 per cent. and upwards	15	5,302,000	18	5,828,000
,, ,, 15 to 20 per cent.	20	5,439,000	28	12,684,000
,, ,, 10 to 15 ,,	36	14,057,000	44	21,916,000
,, ,, 5 to 10 ,,	36	14,182,000	15	6,620,000
,, ,, less than 5 ,,	3	1,350,000	4	564,000
Banks	110	40,331,000	109	47,632,500

This great accumulation of capital in joint-stock banks has taken place during the short period of fifty-three years.

It is to be hoped that these banks will steadily progress, not forgetting to increase their reserves in proportion to an increase of liabilities.

It is desirable that a uniform balance sheet should be published by all the joint-stock banks in England and Wales, because it would be of great advantage to the commercial world, as well as to the banks, which could by comparison gain some valuable information. Thus any defects in the management might possibly be discovered and remedied.

CHAPTER IX.

THE PRIVATE BANKERS.

THE private bankers are steadily decreasing in this country. This is seen from the following table:—

1808 = 600
1810 = 721
1844 = 335 and 93 branch offices.
1875 = 251
1894 = 101 and 464 ,, ,,

	1860.	1865.	1870.	1875.	1894.
Purely London Bankers, -	53	46	47	55	21*
Provincial ,, -	239	211	207	196	80
	292	257	254	251	101

In the year 1878 four private bankers stopped payment, thus still reducing their number.

LONDON PRIVATE BANKS.

1810 = 40 Clearing House.
1845 = 26 ,, ,,
1858 = {25 Clearing Bankers. 22 Non-Clearing Bankers.
1866 = {14 Clearing Bankers. 18 Non-Clearing Bankers.
1872 = {13 Clearing Bankers. 17 Non-Clearing Bankers.
1878 = {12 Clearing Bankers. 18 Non-Clearing Bankers.
1895 = {5 Clearing Bankers. 16 Non-Clearing Bankers.

This great decrease has been caused partly by amalgamation and partly by the banks becoming extinct. When

* The recent amalgamation of banks with Messrs. Barclay & Co. will reduce the number to 20 and 68 respectively.

a private bank becomes extinct its place is generally taken by a joint-stock bank. There seems to be a tendency to have a small number of large private banks which become larger, whilst the business of smaller banks gradually diminishes.

The capital at the disposal of the London private bankers was estimated in 1834 at £29,500,000, of which the sum of £3,000,000 belonged to the country bankers. Mr. Dun estimated in 1876 that the money lodged with the London private bankers amounts to £80,000,000 and with the country private bankers to £93,500,000.

The private bankers of the present day are men of known wealth and position, and this, combined with their intimate knowledge of banking, has been the cause of their great success.

Several of the large private banks in London occupy an eminent position in the commercial world.

In recent years the private bankers have taken a very wise step by publishing balance sheets. The first bank to do this was the firm of Messrs. Glyn, Mills, Currie & Co. This policy has proved eminently successful, because it has shown that the private banks have large capital and reserves in proportion to their liabilities.

CHAPTER X.

BANKING IN SCOTLAND.

THE Bank of Scotland was the first bank formed in that country. It obtained an Act from the Scotch Parliament on 17th July, 1695, which authorised the Crown to grant a Charter of Incorporation. Unlike the Bank of England it was not connected with the State, although it possessed a monopoly of banking for twenty-one years. This bank did not at first receive money on deposit, and its profits depended entirely upon the note circulation.

The next bank formed was the Royal Bank of 1727. Its promoters complained that the Bank of Scotland charged too high a rate of interest for loans; that it was hostile to the House of Hanover; that it was very exacting with regard to the securities required, and that loans on its own stock were not allowed.

The formation of this bank abolished the monopoly of the Bank of Scotland.

The British Linen Company was formed in 1746 for carrying on the business of linen manufacturers as well as of banking. The former business was soon, however, relinquished.

The next bank formed was the Ayr Bank. Its promoters supposed that they could issue notes to an unlimited extent, but this popular delusion was soon dissipated. After issuing £800,000 of paper money, the bank was unable to pay the notes on presentation. In

the year 1772 it stopped payment, and the effect of its suspension was so great that only three of the then existing private banks survived the panic.

Although there are now no private banks in Scotland, yet there were eight in existence in 1819.

The following table shows the increase in the number of banks and branches :—

1819 = 30	chief offices and	97	branches.
1830 = 27	,,	145	,,
1845 = 20	,,	376	,,
1864 = 13	,,	591	,,
1878 = 12	,,	940	,,
1894 = 10	,,	1008	,,

The number of offices in proportion to the inhabitants is larger in Scotland than in England or Ireland. Thus :—

No. of offices in	1826 = 167	or 1 to every	13,170	inhabitants.
,,	1841 = 380	,,	6600	,,
,,	1856 = 585	,,	5230	,,
,,	1872 = 790	,,	4250	,,
,,	1883 = 898	,,	4260	,,

Although the facilities for banking are greater in Scotland than in England, yet on the other hand the working expenses must tend to lessen the profits of the banks.

The great success of Scotch banks is supposed to be due to the following circumstances, *viz.*: 1st, banking in that country was not originally a monopoly, although the privilege of note issue made it so at a later date; 2nd, it was treated as an ordinary business in which the State was only indirectly concerned; and 3rd, the only restrictions were, that the banks should confine themselves to banking.

The Act of 1845 relating to Scotland stated that no new bank of issue should be formed in that country, and this practically prevented new banks opening, because the issue of notes is an essential part of Scotch banking. Since the Act was passed, seven banks of issue have ceased to exist,

viz., Aberdeen Bank, Dundee Bank, Eastern Bank, Edinburgh and Glasgow Bank, Perth Bank, Western Bank, and City of Glasgow Bank.

We have already noticed that the issue of £1 notes was allowed by the Act of 1845 and also that the Scotch circulation has far exceeded the authorised limit. This Act also prevented other banks from being formed, and consequently we have large institutions with correspondingly great liabilities. If at any time a bank failure should occur in the country the effect would be most disastrous. No doubt there would have been more banking institutions in Scotland if the existing banks had not practically a monopoly.

Another feature of Scotch banking is the system of deposits. Small amounts are received, and consequently the banks assume the character of savings banks for the country. Banks are able to take these small amounts partly in consequence of a high rate of interest ruling in Scotland. The great prosperity of the Scotch people has, however, been attributed to the system of deposit banking.

This concentration of capital at places where it is most required must materially benefit any country and increase its wealth.

In Scotland there are more shareholders in banks in proportion to the inhabitants than in England or Ireland. The Scotch people have great confidence in their banking institutions.

For example:—

England . .	1 share to	416 persons.
Ireland . .	1 ,, ,,	433 ,,
Scotland . .	1 ,, ,,	253 ,,

By this means runs on the banks have been prevented in times of panic and commercial disaster.

The people are, therefore, more directly interested in

the banks, and consequently in times of panic and commercial disaster do not lose confidence.

The system of cash credits is another peculiar feature of Scotch banking. Any person who can obtain two sureties who are willing to give a bond, is allowed to draw against the amount placed to his credit at the bank. The sureties have a right to inspect the bank books in order to see that the account is in strict accordance with the bond.

The progress of money lodged has not been so rapid as in England. Thus:—

	£
1826	= 21,000,000
1841	= 27,000,000
1844	= 33,192,000
1855	= 43,271,000
1865	= 56,185,000
1875	= 78,405,000
1895	= 93,489,068

The following is a list of the banks now in existence:—

		Paid-up Capital. £	Reserve. £
Bank of Scotland . .	1695	1,250,000	800,000
Royal Bank of Scotland .	1727	2,000,000	754,879
British Linen Company .	1746	1,250,000	1,400,000
Commercial Bank . .	1810	1,000,000	675,000
National Bank of Scotland	1825	1,000,000	785,000
Union Bank of Scotland .	1830	1,000,000	505,000
Clydesdale . . .	1838	1,000,000	545,000
Aberdeen Town and County	1825	252,000	134,000
North of Scotland . .	1836	400,000	50,000
Caledonian . . .	1838	150,000	69,000
		9,302,000	5,717,879

The Bank of Scotland, the Royal Bank and the British Linen Company are chartered banks and limited in their liability to the public, their corporate property being alone liable for debt. The remaining banks are limited.

The total liabilities of these banks amount to £120,337,697 and their cash and Government securities to £53,200,000.

The ratio of cash in hand and money at call is about 17½ per cent.

The note circulation of the Scotch banks is equal to about 50 per cent. of their capital and reserve fund.

That the Scotch people are prudent, saving, and industrious is shown by the cash deposits, which amounted a few years ago to £90 per head of the adult male population. This is a far greater proportion than in England or Ireland.

The Scotch banks are to be commended for publishing a complete balance sheet, which enables us to show clearly the progression of banking in that country:—

11 Banks. LIABILITIES.

	Deposits.	Notes.	Acceptances and Drafts.	Total Liabilities.
	£	£	£	£
1865	57,140,000	4,986,946	2,668,881	64,796,247
1869	63,820,000	5,390,947	4,296,319	73,508,077
1894 (10 banks).	93,489,068	6,733,523	2,981,638	120,337,697

ASSETS.

	Banking Advances.	Stocks and other Secs.	Banking Premises.	Reserves.	Total Assets.
	£	£	£	£	£
1865	54,878,548	3,925,530	1,091,862	17,297,925	77,193,871
1869	61,095,648	4,037,530	1,187,114	20,114,153	86,434,559
1894 (10 banks)	60,743,952	31,068,042	6,359,933	22,165,770	120,337,697

The following abstract of balance sheets from 1870 to 1877 is taken from seven banks, *viz.*, Bank of Scotland, Royal Bank, British Linen Company, Commercial Bank, National Bank, Union Bank, Clydesdale and City of Glasgow Bank:—

	Due to Proprietors.		Due to Public.			Assets.		Total Assets.	Net Profits.
	Capital.	Reserve.	Circ.	Deposits.	Accepts.	Cash, etc.	Disc'nts.		
	£	£	£	£	£	£	£	£	£
1870-1	8·77*	3·51	5·85	59·60	4·11	23·16	59·79	81·95	1109
1874-5	9·00	3·46	7·46	74·27	5·05	27·62	72·68	100·30	1284
1875-6	9·00	4·49	6·86	74·37	5·72	27·49	73·38	100·87	1275
1876-7	9·00	4·98	6·84	73·83	6·24	28·95	72·65	101·30	1287
1894 (10 banks)	9·00	5·71	6·73	93·48	2·98	22·16	60·74	120·33	936

These tables show—

(1) That in every case but two there has been an increase in the note circulation of £1,000,000.

(2) An increase of deposits in twenty-four years of £34,000,000.

(3) There has been a decrease in acceptances from £4,110,000 to £2,980,000.

(4) The net profits of the Scotch banks show a decline, as is the case with the English banks.

There was a decrease in deposits in consequence of the failure of the City of Glasgow Bank. This is shown from the following statement:—

May 18, 1878	£78,000,000
October 19, 1878	78,000,000
May 17, 1879	67,000,000

The latest reports of the banks show, however, that the deposits are steadily increasing.

Another feature of Scotch banking was the allowance of interest on current accounts, which somewhat differs from the procedure of the majority of English banks. Interest was formerly allowed on current account by some of the English banks, but the system was abandoned because with increasing competition it was found to be unprofitable.

In 1863 the Scotch banks fixed the rate for daily

* 0·000's omitted from columns 2 to 9 and 000's from column 10, thus £8·77 = £8·770·000.

balances from $1\frac{1}{2}$ to 4 per cent., and for minimum balances from 2 to $4\frac{1}{2}$ per cent.

The interest for advances from 1822 to 1864 was never below 4 per cent. :—

1847 = $5\frac{1}{2}$ per cent.	1863 = 7 per cent.
1856 = 6 per cent.	1864 = 8 and 9 per cent.
1857 = $6\frac{1}{2}$ per cent.	

An account of the progress of the Scotch banks would be incomplete without reference to the great banking disasters in 1857 and 1878.

It was thought that banking in Scotland was safe and prosperous; in fact, some believed that the failure of banking institutions in that country was impossible. This delusion was dispelled by the great failures of 1857 and 1878. These great disasters showed that Scotch bank directors could act in a reckless manner like directors of other companies. The failures of the Western Bank of Scotland in 1857, and the City of Glasgow Bank in 1878, were very similar in character. In 1857 the Western Bank lent to four or five private firms a sum equal to its capital. This bank had also an agency in New York, and a large proportion of its deposits was sent there to support all kinds of speculation. When, however, speculation in America experienced a sudden check, the Western Bank found itself in the possession of a large amount of worthless securities. The bank was unable to meet its liabilities, and consequently had to close its doors. It was ascertained that the capital of £1,500,000, the reserve fund of £227,000, and £916,864 6s. 8d. in addition were lost. The failure of such a large bank caused a run upon all the others, but by giving credit and paying the notes of the bankrupt bank it was soon stopped.

The City of Glasgow Bank suspended payment for a short time in 1857, but judged by later events it would

have been better if it had never opened its doors. The failure of this bank in 1878 was very disastrous, because the English as well as the Scotch banks felt the effects of the suspension.

Shareholders of banking institutions in both countries saw how easy it was to be deceived. The accounts of the Glasgow Bank had been falsified from the year 1873. The liabilities of that bank were £2,000,000 more than stated in the balance of 5th June, 1878, whilst the assets were nearly £5,000,000 less, namely :—

Bills of exchange	£2,400,000	less than stated.
Advances on heritable property . .	50,000	,,
Cash on hand	400,000	,,
Government stocks, etc.	1,700,000	,,
	£4,550,000	

Deducting the capital and reserve, £5,190,983 11s. 3d. had to be provided by the shareholders of the bank.

The Act of 1845 stated that the excess in the circulation above the authorised issue should be provided for by gold, but for some time the Glasgow Bank had made false returns to the Government, because it did not hold sufficient gold to represent the excess.

No doubt Sir Robert Peel intended that the gold held should be a cover for the note issue, but it seems that the Act of 1845 was a failure in this respect. The other banks promptly met the disaster by paying the notes of the Glasgow Bank, and also by giving every facility to those who had money locked up in that bank. The business of the City of Glasgow Bank was conducted in a very bad manner. The directors lent large sums of money to their own firms; no less than £5,800,000 was lent to four commercial houses in which they were interested. They also supported rotten concerns which every day were becoming more insolvent, and issued bills

supposed to be drawn in Melbourne but in reality at Glasgow. As a last resource they invested large sums of money upon land in Australia and New Zealand, thus hoping to retrieve their position. It is important to remember that when the City of Glasgow Bank's acceptances were refused in London, the bank was really doomed and its doors were closed within a week. This shows the danger that may arise from any bank having too many acceptances in the market. Although this great failure depreciated the value of bank shares, and also caused a large withdrawal of deposits, yet it was not without its advantages, because it was the means of clearing away insolvent houses.

Banking was brought prominently before the public, and many important questions relating to that subject were discussed with a view to certain reforms being carried out.

The opening of London offices by Scotch banks has excited a great deal of interest in this country.

The following Scotch banks have opened London offices :—

Bank of Scotland	opened in	1869
Royal Bank of Scotland	,,	1875
British Linen Company	,,	1877
National Bank of Scotland	,,	1867
Union Bank of Scotland	,,	1868
Clydesdale Banking Company	,,	1877

It has been stated that the Scotch banks have not shown their usual prudence by opening offices in London for the following reasons :—

(1) They had in their own country a prosperous and sound business, with profits and dividends considerably increasing.

(2) That the scheme of opening London offices is a departure of the most marked kind from the maxims which have hitherto guided them.

(3) That the Scotch banks assuming responsibilities of London institutions must remodel their reserve funds.

The *Scotsman* of March, 1878, stated "that the experiment of raising deposits in Scotland and using them in London will be watched with interest".

Another point in connection with the opening of London offices was the large increase in the acceptances of those banks. This kind of business must always be carried on with great caution. In times of commercial distrust there is the possibility that the credit of any bank may be affected by the amount of its bills circulating in the market. The securities also held as cover may depreciate in value.

The following table shows the increase in the acceptances of Scotch banks from 1870 to 1877 :—

	1870-1.	1876-7.	Increase.
	£	£	£
Two banks with London offices .	2,220,000	3,620,000	1,400,000
City of Glasgow Bank	770,000	1,350,000	280,000
	3,000,000	4,970,000	1,670,000
Five other banks	1,120,000	1,770,000	630,000
	4,120,000	6,740,000	2,300,000

In 1876-7 these acceptances were equal to one-fourth of the total acceptances of the London joint-stock banks, but there has been a great decrease in recent years. It seems an anomaly to allow Scotch banks of issue to open branches in London when English country banks have to forfeit their note circulation if they do the same thing.

The National Provincial Bank gave up its issue on opening in London, losing thereby £10,000 per annum. Besides this the Scotch Act of 1875 gave the banks considerable privileges, which practically secured for them the monopoly of banking in that country.

Mr. Goschen in 1875 introduced a bill to prevent the Scotch banks from opening in London, but this met with

considerable opposition and was abandoned. A clause was inserted in the Banking Bill of 1878, stating that all banks opening in London should forfeit the right of issuing notes, but this also was struck out before the bill passed.

The dividends paid by the Scotch banks in 1869 were in comparison with the English banks in a lower class, the reason apparently being in consequence of their large capital. If we compare 1869 with 1878 we find that the Scotch banks had considerably increased their dividends, but the period from 1878 to 1894 shows a decrease:—

	1869.	1878.	1894.
Bank of Scotland	12	14	12
British Linen Company	13	14	15
Caledonian Banking Company	10	14	8
Clydesdale	10	14	10
Commercial Bank	13	15	15
National Bank	12	15	15
North of Scotland	10	13¾	6¼
Union Bank of Scotland	10	13	10
City of Glasgow	8	11½	—
Royal Bank of Scotland	8	9½	8

The Scotch banks in 1876 agreed to the following charges:—

(1) Interest on money lodged and on advances and discounts to be fixed at meetings of the banks to be held at Edinburgh.

(2) In addition to the discount a commission of 1s. 3d. per cent. is charged on bills payable in Scotland; on bills payable in London no commission is charged, but elsewhere in England and Wales, 2s. 6d. per cent.

(3) Other fixed charges are made for negotiating documents payable on demand, for granting drafts, making transfers, etc.

CHAPTER XI.

BANKING IN IRELAND.

Banking in Ireland resembles more the English system than the Scotch; because the monopoly of joint-stock banking was given to one institution, *viz.*, the Bank of Ireland, which was formed ninety years after the Bank of England, *viz.*, in 1783.

The Charter of this Bank prevented partnerships of more than six persons being formed in Ireland, and consequently there existed a large number of weak private banks. Many of the latter failed and had a prejudicial effect upon the trade of the country.

In the year 1824 the Bank of Ireland surrendered its monopoly of joint-stock banking beyond sixty-five miles of Dublin, but it was not until the year 1845 that all the restrictions upon banks having more than six partners were abolished. From 1845 any joint-stock bank could have offices in Dublin, but no new bank was allowed to issue bank notes.

The privilege of joint-stock banking was granted to the Bank of Ireland, because that institution lent its capital, *viz.*, £680,000, to the Government, and in the year 1821 a further sum of £500,000 was lent. Thus the capital of that bank was increased to £1,180,000.

In the year 1825 an Act was passed for the purpose of assimilating the currency of Ireland with that of England. Prior to this date an English shilling was valued at 13d., and an English sovereign at £1 1s. 8d.

The Act of 1845 relating to Ireland was very similar to that relating to Scotland. In both countries no new banks were allowed to issue notes, and the existing banks were permitted to retain their £1 notes.

The banking institutions now in existence are—the Bank of Ireland, which is a chartered bank like the Bank of England. It is the Government bank, issues notes, and has numerous branches. The Provincial and National Banks have London offices and issue notes. The Hibernian Bank and the Royal Bank of Ireland do not issue notes.

At Belfast there are three joint-stock banks, *viz.*, the Northern Bank, the Belfast Bank and the Ulster Bank. These three banks issue notes and have numerous branches.

At Cork there is the Munster Bank, which was established in 1865. There are two private banks, *viz.*, Messrs. Guinness, Mahon & Co., and Messrs. Boyle, Low, Murray & Co. All the other private banks have disappeared, although the names of twenty-one appear in the *Post Office London Directory* for 1817.

The eleventh annual report of the Provincial Bank of Ireland for May, 1836, gives a good account of the progress of Irish banking:—

"To show the progress of competition it may be sufficient to state that prior to 1825, when the Act 6, George IV., c. 42, was passed, under which the Provincial Bank was established, the Bank of Ireland had no establishment out of Dublin; that in Dublin itself there were only four more—and these were private banks—and that in all Ireland there were no other than private banks, and those only in Belfast, Cork, Wexford and Mallow. From 1825 to 1834 banking offices in the chief cities and towns of Ireland had been gradually established by the Provincial Bank, the Northern Bank and the Belfast Bank, to the number of about fifty; while within the

short space of the last two years the offices of joint-stock banks having resident managers or agents, beyond fifty miles from Dublin, added to the branches of the Bank of Ireland, have increased to upwards of one hundred and twenty, and appear to be daily augmenting in number. Besides which there are a variety of stations attended on market-days by non-resident agents on behalf of one or other of such banks."

The following table will show the increase in the number of offices:—

1851 = 170 offices or 1 to every	38,300	inhabitants.
1872 = 365 ,, ,,	14,800	,,
1875 = 404 ,, ,,	13,100	,,
1878 = 409 ,, ,,	10,788	,,
1883 = 542 (131 are sub-branches)	9,520	,,
1895 = 493 offices or 1 to every	9,543	,,

In 1877 no less than 39 new offices were opened. This shows that the Irish banks are giving every facility for the deposit of money.

It was impossible some years ago to state the amount of money lodged in all the Irish banks because some of them did not publish any balance sheet, but the following table shows the increase of the private balances in the Bank of Ireland, and the deposits of the Hibernian Bank, the National Bank, the Southern Bank, the Provincial Bank, the Royal Bank, and the Ulster Bank:—

	£
1840 =	5,567,000
1846 =	8,442,000
1852 =	10,773,000
1855 =	12,285,000
1860 =	15,609,000
1865 =	18,619,000
1866 =	20,957,000
1867 =	21,794,000
1868 =	22,168,000
1869 =	22,672,000
1870 =	24,366,000
1871 =	27,348,000
1874 =	31,700,000

All the banks now publish balance sheets, the amount of deposits being £43,612,697.

The year of formation, the paid-up capital, the number of proprietors, and the number of offices of the Irish banks were as follows:—

	Formed.	Offices.	Capital.	Proprietors.	1872 Dividends.
			£		
Bank of Ireland . .	1783	50	2,769,230	—	11
Northern Banking Co. .	1825	44	300,000	718	18½
Hibernian Bank . .	1825	32	500,000	1380	10
Provincial Bk. of Ireland	1825	44	540,000	2000	20
Belfast Banking Co. .	1827	36	250,000	648	36
National Bank . .	1835	106	1,500,000	4000	8
Ulster Banking Co. .	1836	44	250,000	1020	18
Royal Bank of Ireland .	1836	5	300,000	1350	12
Munster Bank, Limited	1864	40	350,000	1163	8

The proportion of paid-up capital and reserve to liabilities of Irish banks in 1875 was larger than that of the English and Scotch banks:—

	Purely London Banks.	London & Provincial Banks.	Purely Provincial Banks.	Scotch Banks.	Irish Banks.
Capital	7·3	7·1	12·1	9·2	14·0
Reserve	2·7	2·9	5·4	3·6	5·6
Total proprietors' funds .	10·0	10·0	17·5	12·8	19·6
Money lodged . . .	73·5	83·2	80·3	76·1	65·5
Note circulation . .	—	—	·9	6·2	14·9
Acceptances . . .	16·5	6·8	1·3	4·9	—
	90·0	90·0	82·5	87·4	80·4
Total	100·0	100·0	100·0	100·0	100·0

The following table shows the present position of the Irish banks:—

	Branches.	Capital Paid up
		£
Bank of Ireland	59	2,769,231
Belfast Banking Company . .	40	400,000
Hibernian Bank	59	500,000
Munster Bank	52	200,000
Nation l Bank	104	1,500,000

	Branches.	Capital Paid up.
		£
Northern Banking Company . .	51	450,000
Provincial Bank of Ireland .	60	540,000
Royal Bank	7	300,000
Ulster Bank	61	450,000

Their deposits amount to £43,612,697, against cash, £10,642,482 and investments £17,644,605.

The banks of Ireland have not suffered so much from failures as the English and Scotch, and appear to be conducted on sound principles. Their business is steadily increasing, although not so rapidly as the English banks. The system of audit of the National Bank ought to be mentioned, because it is worthy of imitation. The shareholders appoint three of their number to inspect the books of the bank, and these can if necessary employ professional auditors to assist them in drawing up their statement. Thus three separate audits of accounts are brought before the shareholders at the annual meeting.

CHAPTER XII.

ACCUMULATION OF CAPITAL IN BANKS.

HAVING briefly considered the progress which the various banking institutions have made, we will now show the enormous increase of deposits in all the banks of the United Kingdom.

Mr. J. G. Hubbard stated that the deposits held by country bankers from 1832-1841 were from £16,000,000 to £20,000,000. In 1847 Mr. Wilson stated that the banks in the United Kingdom were about 1600 and that their deposits amounted to £200,000,000 or £250,000,000. The accumulation in recent years has been very great. Mr. Newmarch in 1850 stated that the deposits of the banks in the United Kingdom were about £260,000,000, and Mr. Palgrave in 1871 estimated the amount as £662,000,000.

Mr. Dun stated in his paper read before the Statistical Society in 1876 that the amount had increased to £782,000,000, as follows:—

London Banks—	
Joint-stock	£93,400,000
Private	80,000,000
	£173,400,000
London and Provincial Banks	60,400,000
Purely Provincial Banks—	
Private Banks } Joint-stock Banks }	256,000,000
Total—England and Wales	£489,800,000
Carry Forward	£489,800,000

Brought Forward	£489,800,000
Scotland	105,900,000
Ireland	48,400,000
	£644,100,000
Bank of England	70,600,000
Discount Houses	67,900,000
	£782,600,000

It must be also remembered that the Foreign and Colonial banks in London have a large amount of capital at their disposal :—

27 Colonial Joint-stock Banks with London Offices,	£156,305,379
22 Foreign ,, ,, ,,	59,466,147

besides 23 Colonial and Foreign joint-stock banks without London offices. This latter class has large sums of money deposited with the London bankers.

Mr. James Dick in a paper read before the Institute of Bankers in 1892 gives the following estimate of deposits in banks for 1891, *viz.* :—

Deposits ascertained	£660,660,000
Savings Banks' deposits ascertained	113,983,000
London Private Banks estimated	50,000,000
Country ,, ,,	50,000,000
Foreign and Colonial Banks estimated	120,000,000
	£994,643,000

We must not forget the rapid progress which the Savings Banks have made since they were established in 1818 :—

		£
Deposits	1820 =	2,915,000
	1841 =	24,474,689
	1851 =	28,931,000
	1860 =	41,258,000

1863 Post-Office Savings Banks opened.

1870	Savings Banks	£37,959,000
	Post-Office Savings Banks	15,099,000
1878	,, ,,	30,412,000
	Trustee Savings Banks	44,293,000

In 1891 the total deposits in Savings Banks amounted to £113,983,000, showing an increase in thirteen years of £39,000,000.

This great accumulation of money in banks during recent years shows the rapid growth of capital in the United Kingdom. Mr. Griffen estimated the capital of the country to be £8,500,000,000. This great increase in the wealth of this country is no doubt partly due to the banks, which have directed capital to enterprises where it can be utilised at a profit. There are, however, some dangers connected with this vast accumulation of money in banks. For instance, we have in this country only one place (*viz.*, the Bank of England) where the sudden requirements of the money market can be met. It is the only place where gold can be obtained in any large quantities to meet a sudden demand. The bankers keep practically their reserves with the Bank of England, and therefore in times of bad credit it has to meet great demands. Although, therefore, the increase in deposits has been very rapid, the increase in the reserves of bankers has been small, partly in consequence of the Bank of England being the bankers' bank.

Of course, it is impossible to meet all liabilities on demand, yet it is necessary for banks always to have sufficient reserves to meet any sudden withdrawal of deposits. Again we know that large reserves are necessary during periods of financial distrust, when it is desirable that good mercantile firms should be able to obtain accomodation.

CHAPTER XIII.

BANKING AND COMMERCIAL CRISES.

WE shall now consider certain periods in the history of banking when its progress has been retarded. The great foundation of our banking system is confidence, but when by reckless speculation on the part either of banks or of the commercial world there exists distrust, the result may be disastrous both to banking and commerce.

The history of English commerce shows great fluctuations in prices of commodities, in accordance with the laws of supply and demand. If any great catastrophe affects one industry, the effect is in time felt by other industries. This is partly due to the division of labour, which is the outcome of the expansion of trade. Manufacturers are able to produce goods in large quantities at a reduced cost in consequence of the division of labour. This cheapening process increases the demand for commodities. On the other hand, we must not forget that the system has its disadvantages, because trades become more dependent upon one another. For example, we know how dependent the iron industry is upon that of coal. The result is that the producer and consumer are not brought into contact with each other, and consequently when one fails a great number of intermediaries are affected.

We know that depressed agriculture causes stagnation in trade, because it is still a large industry in this country. Banks in agricultural districts are considerably affected when that industry is depressed.

If there is a series of bad harvests there is a less amount of capital to be spent upon other industries, consequently during such periods we should expect to see the deposits in banks decrease.

Credit is singularly varying. It confers advantages, but on the other hand there are corresponding disadvantages.

We have observed in a former chapter the disastrous effect upon banking by the indiscriminate circulation of bank notes, a form of credit which is now strictly regulated by Acts of Parliament.

Again, the use of credit enables capital to be transferred to places where it is more urgently needed. As a rule we might say that capital finds its way to places where it can be utilised with better advantage. Credit also increases efficiency and facilitates the business of the country. It tends to diminish the friction of exchange and steady prices.

We have already noticed that production is stimulated by the use of capital. Another point to remember is, that in times of good credit the bills issued against commercial transactions are taken readily, and consequently years of improving credit are years of rising prices. On the other hand, when credit is bad we find that prices fall.

There are great dangers attending our system of credit, and we shall observe that at various times the banks of this country have not made good use of the capital entrusted to them.*

During commercial crises people exhaust their credit by converting floating capital into fixed. When prices rise, every one is anxious to secure large profits. At such times the liabilities of speculators are increased quite out of proportion to their means, and consequently when they are called upon to meet their engagements are unable to do so.

One of the drawbacks to our present system of credit is that it enables an unsound business to be carried on, and

consequently when the crash comes the effect is great. In fact, we lose in security what we gain in economy. The banks of this country exert a great power, and it must be their constant endeavour to keep aloof from the spirit of speculation. By prudent management they are able to exercise great influence, and consequently assist in the prevention of sudden collapses of credit.

The system of large deposits in banks is peculiar to England. The accumulation of capital affects trade and consequently prices. It has been stated by the late Mr. Bagehot that a rise in prices is caused by cheap money, cheap corn, and improved credit. When this occurs, the banks have a large number of applications for loans, so that the borrower may benefit by the rise. As a natural consequence the rate of interest rises, and generally at a rapid rate. At such times the demand for capital is greater than the supply.

Whenever there exists a speculative mania, the result is a system of over-trading, and consequently liabilities are contracted which cannot always be met. At the same time we generally get an investing mania, brought about by the same causes. It has been truly stated in the excellent book entitled *Lombard Street* that any sudden event which creates a great demand for actual cash may cause a panic in a country where cash is economised and debts payable on demand are large. Accidental events, such as a bad harvest, a failure of firms, etc., cause a sudden demand for cash, and may lead to a panic.

In fact, the characteristic of a true crisis is a previous destruction of wealth. Gold, notes and banks are mere machinery required to carry on our modern system of credit. At each successive crisis attention has been drawn to the system of banking rather than to the fluctuation of trade and the speculative mania of the people.

We must not forget, however, that with the best system of banking it would be impossible for any bank to meet any large withdrawal of deposits. Ricardo says: "On extraordinary occasions a general panic may seize the country when every one becomes desirous of possessing himself of the precious metals as the most convenient mode of realising or concealing his property. Against such panic banks have no security on any system."

The late Professor Jevons endeavoured to account for periodical crises by the appearance of spots on the sun's disc at intervals of 11·1 years. We know that the condition of trade is largely dependent upon the harvests not only at home but abroad.

It seems that the price of Delhi wheat reached a maximum in value every ten years. We know that the amount of heat received from the sun is varying, and may suppose that the crops would vary in the same proportion. "The crops of Western Europe have always been strongly affected by communication with the Indies. Several of the crises are distinctly traceable to this cause, especially those at the beginning of the eighteenth century. That was a time of wild enterprise in the tropical regions, as the very names of the South Sea Company, the Mississippi Scheme, the Darien Project, etc., show. The Dutch, English, and French East Indian Companies were then potent bodies, the constant subject of legislation and controversy. Thus it is my present belief that to the trade with India, China, and probably other parts of the tropical and sub-tropical regions, we must attribute the principal fluctuations in European commerce. Surely there is nothing absurd in such a theory when we remember that the present crisis is at least partly due to the involvement of the City of Glasgow Bank in the India trade, through the medium of some of their chief debtors. Thus the

crisis of 1878 is clearly connected with the recent famines in India and China, and these famines are confidently attributed to solar disturbance."

It would be interesting if we could judge of Professor Jevons' opinion on the state of banking and commerce at a recent period, when there was an abundance of corn at a very low price concurrent with a certain stagnation in trade.

It is beneficial to the community that banks which lend money to unsound borrowers and also foster undue speculation should fail, but unfortunately, on the other hand, many good institutions suffer in consequence of a loss of credit. The cause of these disasters to banking and commerce is principally due to excessive speculation, which results in a crisis or panic.

Whenever we get in this country a rapid accumulation of capital, it is usually accompanied by a great demand for investments, and this sometimes leads to speculative enterprises. For example, capital is expended say in making railways, digging mines, or constructing docks, and would not be reproduced for a long period of years. In order to carry out such enterprises, loans are contracted at banking institutions, and when the time for repayment arrives the borrowers are unable to meet their liabilities. If capital has been sunk in the manner already indicated there is no great accumulation of it in banks, and consequently the bankers' power to lend is diminished. When merchants cannot obtain assistance in order to meet losses or calls on new undertakings they begin to lose confidence in each other, and then we get the culminating point of a crisis, *viz.*, a panic, when suspicion rests upon every one. At such times depositors in banks may demand repayment of their capital, and thus banks are suddenly

called upon to meet an additional strain upon their resources.

It is questionable whether it is desirable for banks to largely encourage the system of deposit accounts, because when a feeling of distrust exists in the money market the depositor is the first to demand his money. This was clearly shown in the recent Australian bank crisis. It was also formerly considered by private bankers that it was not the duty of a banker to find an investment for depositors' money. Even at the present time, some banks refuse to take deposits except from their customers.

If bankers have lent money to persons for the purpose of speculation, then they may possibly find themselves in possession of a large quantity of worthless securities which are unmarketable. On the other hand, if they have advanced money on good securities which are saleable, they stand a much better chance of surviving the crisis. At these critical periods the people refuse to see that gold, notes, banks, etc., are mere machinery, and that the crisis is quite distinct from such questions.

It will be important to notice the position and action of the Bank of England during commercial crises, because the returns of that institution give us a good record as to the course of events in the money market. The Bank has been called upon at such times to exercise its great power in order to restore confidence and also to allay the panic which generally occurs. When a withdrawal of deposits from other banks has taken place, those of the Bank of England have generally increased, showing that at such times confidence in the Bank remains.

We will now consider these crises in chronological order.

The first run upon bankers took place when the Dutch

sailed up the Thames in 1667. The South Sea Company, which was formed in 1711 for the purpose of trading in the South Seas, was for a time a rival of the Bank of England; and when we consider that the latter institution was in difficulties in the years 1704 and 1709, we can imagine that such was the case.

The South Sea Company, by means of advertisements representing enormous advantages, managed to get the price of its stock raised from £290 on 7th April, 1721, to £890 on the 2nd June, but it fell rapidly and was quoted at £400 on 2nd September. Many of the goldsmiths and bankers had advanced money upon South Sea stock, and when the price of the stock rapidly fell, a run upon the banks occurred. Many stopped payment, and some of the bankers absconded. There was also a run upon the Bank of England, but by a clever scheme it was stopped.

The success of the Pretender in Scotland in 1745 caused a disturbance of credit, when the notes of the Bank of England fell to 10 per cent. discount.

The year 1763 was remarkable as being the first of a series of commercial crises caused by a too great expansion of credit. A large number of failures amongst the merchants of Hamburg affected those trading with that place, and in order to stop the panic the Bank of England made advances to the extent of £1,000,000.

The commercial speculations of 1772 created another panic; this was exemplified by the number of bankruptcies, which amounted to 525. The failure of Messrs. Heale & Co., bankers in Threadneedle Street, intensified the panic, and consequently the Bank of England's aid was necessary to restore confidence.

After the close of the American War in 1782, a large expansion of our foreign trade occurred. Speculation became active, and this combined with an injudicious

issue of notes by the Bank caused a drain of specie, which almost caused it to suspend cash payments. It is stated that the country bankers supported all kinds of wild projects by means of the issue of bank notes, and when called upon to pay them were unable to do so.

In the panic of 1793 no less than 100 out of a total number of 400 country banks stopped payment, and the remainder were in a critical condition. The commercial crises were attributed to the monopoly of the Bank of England, combined with its restricted issue of notes at times when a stringency of the money market existed. The fact of a previous destruction of wealth, combined with a depreciation in the value of commodities, was overlooked. No doubt the private bankers supported speculation by the issue of notes, but this was not of itself sufficient to cause a crisis.

The discussions on the currency, however, had a good effect, because the Bank Charter Act of 1844, which secured the convertibility of the note, was the outcome of such deliberations.

After the American War there was a period of prosperity throughout Europe. The usual course of events followed, *viz.*, an era of speculation. This was shown by the Bank of England's note circulation, which rose from £6,000,000 in 1784 to £11,500,000 in 1792. In the autumn of the latter year a series of failures occurred. On the 15th February, 1793, a house of considerable magnitude, deep in corn speculations, failed, and on the 19th the Bank of England refused to discount the bills of Lane, Son & Fraser, and that firm suspended payment next day with liabilities of nearly £1,000,000. A great number of respectable firms were involved through this failure. In the meantime the panic affected the bankers. The failure of banks commenced at Newcastle, and although the

partners in the banks at that place were opulent, yet their assets were locked up in securities which could not be realised, and consequently they were obliged to suspend payment. The banks of Exeter and of the West of England were almost the only institutions which survived the crisis.

The failures were attributed to houses issuing notes without a sufficient reserve.

A committee of the House of Commons recommended the issue of exchequer bills, which was adopted by the Government and had the effect of restoring confidence. When it was known that capital could be borrowed then the alarm subsided.

The next banking crisis occurred in 1797, when some banks at Newcastle were in difficulties, and the situation became so critical that an Act was passed allowing the Bank of England to suspend payment. It was thought that the laws affecting the Bank of England and also of the currency were the cause of financial troubles, but as Professor Jevons states at a later period: "I must maintain then that under the present system the English currency is governed by the natural laws of supply and demand of a metallic currency and not merely by artificial regulations. If the terms are interpreted aright we have already a natural and free trade system of currency, and I venture to take this auspicious expression free trade from those who use it wrongly, and who confuse the free manufacture of currency with free trade in *capital*, the true business of the banker."

In 1807 the South American Continent became independent, and speculation with that country was soon at its height. It is stated that clerks with about £100 capital were allowed by the banks to have discount accounts amounting from £5000 to £10,000. By such

means the bankers supported speculations, and consequently credit sustained a shock in 1810.

We have the following report of it: "The failures of houses of the highest respectability both at London and at different provincial towns of Great Britain have within the last month (August, 1810) been unprecedented in number and importance. A West India broker who had been considered the first in his line was, we are told, the prime cause of the stoppage of a banking house whose credit was previously unimpeached. The several banks in the country connected with the London house of course shared his fate, and from them the evil spread to merchants and manufacturers, traders, and in short to the very servants and dependants of these. . . . Speculation in Spanish wool, an article which has fallen about 50 per cent., was considered as the origin of the unlooked-for disaster."

Fourteen years later, *viz.*, in 1824, speculation was again active. The people had entirely forgotten their losses through lending so much capital to South America. A large number of companies were floated for constructing railroads, mines, canals, gas, etc., in number about 624, with a nominal capital of £372,000,000. This was followed by a rapid rise of prices, but in a very short time there was a corresponding fall.

The bankers lent money to persons who speculated in all kinds of commodities. They were able to do this by means of issuing a large amount of bank notes, which however they could not pay on demand. Unbounded credit was followed by distrust, and a run upon the banks quickly followed. The Bank of England very unwisely refused to discount any more bills, and this intensified the crisis, which culminated in a panic.

On the 22nd November, 1825, Sir W. Elford's bank at

Plymouth stopped payment, and this was followed by Wentworth & Co., a great Yorkshire firm, the well-known house of Messrs. Pole & Co., besides three or four more London banks and sixty-three country banks. On the proposition of the Government, the Bank of England issued £1,000,000 of £1 notes, which fortunately happened to be in their possession, and also lent large sums by means of discounting bills. These measures afforded great relief to the merchants in London.

The Bank of England's note circulation rose from £19,000,000 (August, 1825) to £25,000,000 (February, 1826).

The bankers suffered immensely from want of confidence, and they tried every possible scheme to stop the run.

A Cambridge bank advertised that it would afford every facility to the holders of its notes for the purpose of having them exchanged for gold or notes of the Bank of England.

An Oxford bank showed so much gold on its counter that every one was satisfied as to its position, and one at Norwich stopped the run by displaying large quantities of Bank of England notes upon its counter.

The following tables will show the fluctuations in prices and the effect of the crisis on the Bank of England :—

SHARES IN 1824.

		Dec. 10, 1824.	Jan. 11, 1825.
	£		
Anglo-Mexican	10 paid	33 pm	158 pm
Brazilian	10 ,,	10 dis	70
Columbian	10 ,,	19 pm	82
Real del Monti	70 ,,	£530	£1350
United Mexican	10 ,,	£35	£155

	July to Nov., 1824.	Dec., 1824, to June, 1825.	Jan. to June, 1826.
Cotton per lb.	7¼d. to 9d.	1/4 to 1/6¼	6¼d. to 7¼d.
Indigo	10/4 to 12/10	21/ to 24/	13/6 to 15/6
Spices (Cinnamon)	6/9 to 7/	11/6 to 12/	6/ to 6/9
Tobacco	2/ to 7/	3/ to 9/	3/ to 8/6
Silk	16/6 to 23/	18/ to 29/10	13/3 to 16/
Sugar	29/11¾	41/5	28/7¼
Coffee	58/ to 60/	76/ to 79/	47/ to 49/
Saltpetre	19/ to 20/	34/ to 36/	22/ to 24/
Iron	£6 to £7	£11 to £12	£8 to £9
Lead	£23	£30	£22

SYNOPSIS OF CRISIS OF 1824.

Date.	Notes under £5.	Notes of £5 and Bank Post Bills.	Total Circulation.	Bills Discounted.	Bullion.
	£	£	£	£	£
1822, 31st Aug.	855,330	16,609,000	17,464,000	3,388,000	10,100,000
1823, 28th Feb.	681,500	17,716,000	18,392,000	4,107,000	10,400,000
,, 30th Aug.	548,500	18,683,000	19,231,000	2,801,000	12,600,000
1824, 28th Feb.	486,130	19,251,000	19,736,000	2,227,000	13,800,000
,, 31st Aug.	443,140	19,689,000	20,132,000	2,449,000	11,700,000
1825, 28th Feb.	416,730	20,337,000	20,754,000	2,466,000	8,700,000
,, 31st Aug.	396,340	19,002,000	19,398,000	5,486,000	3,600,000
1826, 28th Feb.	1,375,250	24,092,000	25,467,000	9,597,000	2,400,000
,, 31st Aug.	1,161,000	20,402,000	21,500,000	2,950,000	6,700,000

The country soon recovered from the effects of this crisis, and scarcely ten years had elapsed before the mania for speculation was again rife.

There were a large number of joint-stock companies formed for the following projects, *viz.:* banks, railways, canals, gas, mining, insurance, etc. During the years 1836-1837 between 300 and 400 companies were formed.

In America there was a great deal of speculation, which led to the failure of 250 houses in 1837.

The Bank of England was censured for its conduct during this crisis. It refused to discount all bills bearing the indorsements of joint-stock banks. It also sent orders to Liverpool stating that no merchants dealing with the United States were to be allowed to have their bills discounted. This action on the part of the Bank of England intensified the panic. The bullion in the Bank rapidly decreased :—

			£
January, 1834	Circulation	. . .	18,000,000
	Bullion	. . .	9,500,000
,, 1836	Circulation	. . .	18,000,000
	Bullion	. . .	4,500,000

SYNOPSIS OF CRISIS OF 1837.

Date.	Circulation.	Bullion.	Bills Discounted.
	£	£	£
1834, 25th February . .	19,050,000	9,225,000	1,800,000
,, 26th August . . .	19,195,000	7,303,000	2,500,000
1835, 24th February . .	18,510,000	6,289,000	2,100,000
,, 25th August . . .	18,085,000	6,255,000	2,600,000
1836, 20th February . .	18,181,000	7,787,000	2,900,000
,, 30th August . . .	18,018,000	5,250,000	4,400,000
1837, 28th February . .	18,165,000	4,077,000	11,200,000
,, 29th August . . .	18,827,000	6,548,000	5,100,000
1838, 27th February . .	18,925,000	10,471,000	3,200,000
,, 28th August . . .	19,488,000	9,540,000	2,900,000

This crisis was followed by another in 1839. A succession of bad harvests, the financial condition of America, and the bad state of credit all over Europe were the cause of it.

In September of that year the bullion in the Bank of England was reduced to £2,816,000, and the Bank was obliged to borrow £2,000,000 from the Bank of France in order to strengthen its position. The rate of discount rose from 3½ per cent. to 6 per cent. (October).

Prior to the passing of the Bank Act of 1844, it was the custom of the Bank to keep one-third of its liabilities in gold. When the Act was passed in 1844, it was supposed that all these commercial disasters which had affected banker and trader alike would entirely disappear. Unfortunately, three years later it was discovered that panics, destruction of capital and high rates of interest would occur from time to time, just as was the case prior to the passing of the Act.

Some people believed that the laws regulating the issue of bank notes were the cause of those events which affected the trade of the country. They believed that if the note circulation was placed on a satisfactory basis, no

more panics, etc., would occur. The real cause of these disasters was, unfortunately, not studied. We have already mentioned that many errors have arisen in consequence of questions relating to banking and currency being treated together.

This was shown in the crisis of 1847, when Sir Robert Peel's Act was attacked on all sides. No doubt the opposition was partly due to its promoters. They stated that the Act would work wonders and completely alter the commercial transactions of the country.

The crisis of 1847 was very similar to those which had previously occurred. A great accumulation of capital led to a great want for new investments. This increase of capital was shown by the large amount of bullion in the Bank of England, Government Stock being at par, and also by low rates of interest.

The following were the rates:—

7th September, 1844, to 11th October, 1845 = 2½ per cent.; then 3 per cent., 3½ per cent. back to 3 per cent., and rising to 4 per cent., 23rd January, 1847.

Mr. Cotton, the Governor of the Bank of England, stated that the true cause of the crisis was the great number of investments in speculative enterprises, more than the capital of the country would permit, the proportion of fixed to floating capital being far too great.

These speculative enterprises were chiefly in railways, cotton and iron. The failure of the potato crop in Ireland and a deficient harvest in this country required more capital, but owing to the previous lock up there was a deficiency.

The large imports of grain from abroad caused a sudden fall in prices and led to the failure of many houses in Mark Lane. The Bank of England refused to lend money on stock or exchequer bills, and credit was very much shaken. This led to the failure of many banks, including the

Royal Bank of Liverpool, the Liverpool Banking Co., and the Union Bank of Newcastle.

The London merchants asked the Government to suspend the Bank Act, and when this was agreed upon, the mere announcement had the desired effect in restoring confidence, although no infringement of the Act occurred. It seems to be the best policy for the Bank of England to lend freely during times of commercial crisis. If people know that money can be obtained at a price, they are not so eager to get accommodation. By such means a crisis may not develop into a panic.

The Bank of England raised its rate from 5 per cent. to 5½ per cent., and finally to 8 per cent. The discounts of that institution increased to an enormous extent:—

		£
Discounts—1844	. . . . . .	2,000,000
	2nd October, 1847	10,000,000
	9th ,, 1847	11,000,000
	23rd ,, 1847	12,500,000

The reserve was reduced from £3,409,000, 2nd October, 1847, to £1,176,000, 30th October, 1847.

SYNOPSIS OF CRISIS OF 1847.

Date.	Circulation.	Bullion.	Reserve.	Bills Discounted.	Rate.	Amount of Exports.
	£	£	£	£		£
1841, 27th Feb.	16,411,000	4,400,000	...	...	5	...
,, 31st Aug.	17,530,000	4,800,000	...	...	5	51·500000
1842, 28th Feb.	17,013,000	6,300,000	...	...	4	47·300000
,, 31st Aug.	20,071,000	9,800,000	...	...	5	...
1843, 28th Feb.	20,284,000	11,100,000	...	...	4	52·200000
,, 31st Aug.	19,939,000	12,300,000	...	...	4	58·500000
1844, 29th Feb.	21,148,000	16,200,000	...	...	4	...
,, 31st Aug.	20,480,000	15,315,000	7,732,000	2,141,000	2½	60·100000
1845, 28th Feb.	19,802,000	15,253,000	8,889,000	2,422,000	2½	...
,, 30th Aug.	21,059,000	15,592,000	7,959,000	4,445,000	3½	57·700000
1846, 28th Feb.	20,921,000	13,776,000	6,691,000	13,137,000	3	...
,, 29th Aug.	20,426,000	16,366,000	9,450,000	6,067,000	4	58·800000
1847, 27th Feb.	19,330,000	12,045,000	6,017,000	8,879,000	5½	...
,, 28th Aug.	18,236,000	9,146,000	4,330,000	9,163,000	5	...
,, 2nd Oct.	18,712,000	8,565,000	3,409,000	10,399,000	5	...
,, 9th ,,	18,640,000	8,409,000	3,322,000	10,978,000	5½	...
,, 15th ,,	19,360,000	8,431,000	2,630,000	11,907,000	..	...
,, 23rd ,,	20,318,000	8,313,000	1,547,000	12,492,000	8	...

PRICES OF RAILWAY IRON.

	£	s.	d.	
1843	6	9	4	per ton.
1844	6	14	3	,,
1845	10	15	10	,,
1846	10	6	8	,,
1848	6	2	10	,,

Consols fell to 85.

The next crisis occurred in 1857. This was principally due to merchants who had speculated far beyond their capital by means of fictitious credit. Money was obtained from the bankers by means of accommodation bills, or bills supposed to be drawn against value received.

There was also a great deal of speculation in America, and the failure of many houses in that country directly affected those banks in the United Kingdom which held American bills. No less than 150 banking houses in America failed, and this was the cause of many banks suspending payment in this country. The Boro' Bank of Liverpool, the Western Bank of Scotland, the City of Glasgow Bank, Sanderson & Co., and Dennistoun & Co., closed their doors.

The directors of the Bank of England appealed to the Government for a suspension of the Bank Act. When this was done on 12th November, 1857, the mere announcement had a good effect, because it was the means of restoring confidence. Although the Act was suspended, the notes issued in excess, without any reserve of bullion, only amounted to £800,000. This shows that the suspension of the Act did not in itself do any good, but it was the means of allaying the wild alarm that existed in the country. The loans advanced by the Bank of England on private securities increased from £20,404,C00 to £31,350,000. A high rate of interest was charged, to prevent those who really did not require advances from

obtaining loans. The reserve of the Bank was reduced from £4,606,000, 3rd October, 1857, to £957,000, 14th November, 1857.

PRICES IN 1857.

	July, 1857.	January, 1858.
Bengal Silk	15s. to 33s. 6d.	11s. to 24s.
Tallow	80s.	60s.
Sugar	55s.	35s.
Cotton	7d.	6d.
Tea	1s. 3d.	1s.

Taken generally, a fall of 20 to 30 per cent.

SYNOPSIS OF CRISIS OF 1857.

Date.	Circulation.	Bullion.	Reserve Notes & Coin.	Bills Discounted.	Rate.	Deposits in Chief Banks.	British Exports.
	£	£	£	£		£	£
1850, 23rd Feb.	18,902,000	17,120,000	12,233,000	2,388,000	2½	11,900,000	71·400,000
,, 31st Aug.	19,962,000	16,770,000	11,086,000	2,603,000	4	...	...
1851, 22nd Feb.	18,713,000	14,436,000	9,722,000	4,115,000	3	14,700,000	74·400,000
,, 30th Aug.	19,716,000	14,362,000	8,645,000	5,393,000	2	...	...
1852, 28th Feb.	20,523,000	19,239,000	12,714,000	3,245,000	2	17,400,000	78·000,000
,, 28th Aug.	27,620,000	21,914,000	13,292,000	2,716,000	3	...	...
1853, 26th Feb.	21,990,000	18,191,000	10,200,000	5,845,000	3½	21,300,000	99·000,000
,, 27th Aug.	22,776,000	16,963,000	8,186,000	5,457,000	5	...	...
1854, 25th Feb.	21,690,000	16,286,000	8,386,000	5,049,000	5	25,600,000	97·200,000
,, 26th Aug.	20,018,000	13,635,000	7,587,000	6,319,000	5	...	...
1855, 24th Feb.	19,062,000	13,045,000	7,982,000	6,066,000	3½	28,300,000	95·700,000
,, 25th Aug.	20,042,000	15,546,000	9,503,000	5,751,000	5½	...	...
1856, 23rd Feb.	18,541,000	10,575,000	6,509,000	8,883,000	4½	33,000,000	115·000,000
,, 30th Aug.	20,124,000	12,387,000	6,736,000	4,446,000	6	...	...
1857, 28th Feb.	18,597,000	10,344,000	6,222,000	8,859,000	5½	37,700,000	122·000,000
,, 29th Aug.	19,324,000	11,501,000	6,650,000	7,893,000	8	...	...
,, 24th Oct.	19,766,000	9,370,000	4,077,000	9,636,000	8	...	...
,, 31st ,,	20,372,000	8,732,000	2,804,000	11,105,000	8	...	...
,, 4th Nov.	20,267,000	8,498,000	2,705,000	11,439,000	10	...	...
,, 11th ,,	20,183,000	7,171,000	1,461,000	13,233,000	...	...	...
,, 18th ,,	21,406,000	6,484,000	1,552,000	16,003,000	...	...	...
,, 25th ,,	21,340,000	7,264,000	2,397,000	17,376,000	...	...	...
,, 2nd Dec.	21,102,000	7,356,000	2,728,000	17,788,000	...	...	...

The *Economist* gives the following account of the securities which were circulating in the market:—

"Such securities were a pure speculation on the future, and a speculation subject to one principal and many smaller casualties.

"Take the case of a railway; the line must be finished and placed in actual working before the obligations representing its cost can have any ascertained value at all. An unfinished railway or dock has no value whatever. In the second place the line must not only be finished and actually worked, but in order to impart value to the bonds and shares there must be a positive profit surplus. The difference between securities such as these, wholly dependent upon future and uncertain events to happen at distant and irregular dates and liable to become worthless by the premature stoppage of the undertaking. and the class of securities which long experience has shown to be best suited to the requirements of the bankers and money dealers, is not marked in its character, but so wide and glaring as to prepare any prudent person to expect mischief."

After this crisis trade revived, and a large number of finance companies were formed for the purpose of promoting all kinds of imaginary profits. From 1858 to 1868, 300 companies were formed with a nominal capital of £504,000,000, including for the year 1866 alone, 75 companies with a capital of £61,000,000.

Companies in 1866.	Capital. £
17 Banks	25,000,000
25 Finance	9,000,000
9 Insurance	7,000,000
24 Shipping	20,000,000

The new banks transacted all kinds of business with foreign countries, and their success depended largely upon

the state of trade with those countries. The finance companies advanced money upon all kinds of undertakings through the medium of bills kept in circulation.

The crisis of 1866 was started by the failure of Messrs. Overend, Gurney & Co. This house, which had then been recently converted into a company, was in its earlier days eminently successful. It is stated that in the year 1860 the partners divided £190,000 as profit. Its position in the money market was supposed to be of the highest character, so that the announcement of the failure had a disastrous effect. Lombard Street was impassable, and it was stated that no such panic had taken place since 1825.

Overend, Gurney & Co. had lent money to support all kinds of speculative enterprises, including the building of ships for the increased trade of the country.

The following account gives a graphic description of the great excitement caused by the stoppage:—At midday the panic was at its height. The demand for accommodation at the Bank of England was very great. Its reserve fell to £730,000, although three weeks earlier it stood at £5,844,000. Its loans on private securities increased from £18,507,000 to £33,447,000. The rate of interest rose to 10 per cent., and remained at that figure for 88 days.

The directors asked the Government to suspend the Bank Act. This was granted, and its announcement had the same effect as in former years. Confidence was restored, but no infringement of the Bank Act took place.

The following table will show the bank rate in panic years:—

1797 to 1837, bank rate 5 to 4 per cent.			
1839	,,	6 per cent.	
1847, 2nd Oct.	,,	5½ ,,	panic year.
,, 23rd Oct.	,,	8 ,,	
,, 20th Nov.	,,	7 ,,	

1857, 3rd Oct.,	bank rate	5½ per cent.	panic year.
,, 24th Oct.	,,	8 ,,	
,, 20th Nov.	,,	7 ,,	
1859	,,	2½ ,,	
1860	,,	5 ,,	
1861	,,	6 ,,	
1862 to 1863	,,	3 to 4 per cent.	
End of 1863	,,	8 per cent.	
1864, Sept.	,,	9 ,,	
1866, 25th April	,,	6 ,,	panic year.
,, 2nd May	,,	7 ,,	
,, 9th May	,,	9 ,,	
,, 16th May	,,	10 ,,	

The effect of the panic of 1866 was so great that Lord Clarendon issued a despatch to foreign states, informing them that although the country had sustained serious losses, yet its trade was still *bonâ fide.*

The banks that failed in 1866, besides Barned's Bank at Liverpool, were the following:—

Overend, Gurney & Co.
English Joint-stock Bank.
Oriental Commercial Bank.
New Zealand Banking Co.
Hallett, Ommaney & Co.
Imperial Mercantile Credit.
Commercial Bank of India.
European Bank.
Robinson, Coryton & Co.
Alliance Financial.
Bank of London.
Consolidated.
Agra & Masterman.

Price of Bank Shares.	1865.	Jan. 1, 1866.	May 12, 1866.
Agra & Masterman	86 pm	33 pm	1 dis
Alliance	10½	4½	10
Barned	...	...	...
Bank of London	22	13 pm	15
City	15	12	5½ pm
Commercial of India	7	5	no price
Hindustan	6	8	16 dis
London and County	63	59	47½ pm
Joint-stock	41	36	27
London and Westminster	80	77	70
Union of London	30	39	32

SYNOPSIS OF CRISIS IN 1866.

Date.	Circulation.	Bullion.	Reserve.	Bills Discounted.	Rate.	Deposits in Banks.	Exports.
	£	£	£	£		£	
1863, Feb. 25	19,117,000	14,614,000	9,253,000	7,066,000	4	54,000,000	144·600,000
,, Aug. 26	20,993,000	15,319,000	8,141,000	6,716,000	4	...	...
1864, Feb. 24	19,675,000	13,819,000	8,028,000	7,807,000	7	67,000,000	160·100,000
,, Aug. 31	20,738,000	12,980,000	6,142,000	9,141,000	8	...	...
1865, Feb. 22	19,659,000	14,600,000	8,254,000	7,950,000	5	67,000,000	165·800,000
,, Aug. 30	21,598,000	14,490,000	6,618,000	9,818,000	4	...	...
1866, Feb. 28	20,768,000	13,967,000	7,345,000	7,253,000	7	69,000,000	188·900,000
,, May 2	22,873,000	13,509,000	4,839,000	8,834,000	6	...	...
,, ,, 9	22,345,000	13,156,000	4,950,000	9,249,000	7·8	...	...
,, ,, 16	26,121,000	12,324,000	731,000	13,831,000	9·10	...	...
,, ,, 23	25,469,000	11,858,000	831,000	14,501,000	10	...	...
,, ,, 30	26,019,000	11,879,000	415,000	16,512,000	...	...	...
,, June 6	25,453,000	13,279,000	2,167,000	16,003,000	...	...	...

Since 1866 there have been few bank failures until the year 1878, although in 1875 some of the banks lost large sums of money on accommodation bills.

The following is a list of failures of private joint-stock and foreign banks in recent years:—

1873 = 5
1874 = 5
1875 = 3
1876 = 2
1877 = ...
1878 = 8
1885 = 1

The large number in 1878 included the City of Glasgow Bank, mentioned under Scotch banking, and the West of England and South Wales District Bank. Both of these banks had lent to individual customers large sums of money, quite out of proportion to their capital.

The West of England Bank had lent to one firm nearly £500,000, although its capital was only £750,000. This money was locked up in the worst kind of investment, *viz.*, collieries, mines and iron works. When the directors endeavoured to realise what they had advanced upon those undertakings, they were unable to do so. If they had followed out the rule imposed by law on the

State Banks of the United States, *viz.*, that no bank should advance to any one person an amount exceeding one-tenth of its capital, then it would have been impossible for the bank to have failed with such heavy liabilities.

Many practical lessons can be learnt by studying these commercial disasters. However, it is impossible for banking to progress if large dividends are the sole aim of the banks in the United Kingdom. Merchants cannot obtain capital for speculative purposes unless the bankers did not to a great extent provide it. In times of prosperity credit is abused, and by this means the trader incurs liabilities which he is unable to meet. This leads to a crisis, and then it is found out that capital, not income, has been spent. Capital is sunk on all kinds of undertakings, and cannot be reproduced for many years. In the various crises some of the banks had lent money upon mills, railways, docks, mines and machinery, instead of upon bills representing trade transactions.

Again, large sums of money are advanced upon stocks and shares, and this sometimes gives a fictitious value to those securities. When a sudden fall in prices takes place, the banker is liable to incur losses on these depreciated securities. The cry is raised during crises for more notes, but the trader does not want credit documents, but a sum of money placed to his credit, against which he can draw cheques.

Banking must always be conducted with prudence and caution if it is to progress in this country. A banker must never forget that he may be called upon at any moment to meet large demands.

Again, he ought always to have a good margin on goods against which money is advanced, so as to meet any possible contingency.

Loans should only be granted for short periods, because it is well known that even within a week there are sometimes great changes in trade and credit.

Another important point for the banker to remember is the difference between a marketable and an unmarketable security.

We know that Consols as an investment for banks are good, because the stock can be sold at a moment's notice, even in times of commercial crises. Thus during the Baring crisis large amounts were sold without affecting the price to any great extent.

Again, mortgages of property are not such a marketable security as produce—such as tea, coffee, or sugar, which can be readily sold in the market. It is also always worthy of notice that on the Stock Exchange there are some classes of securities which can easily be sold, whilst others cannot be realised sometimes for months. Again, other securities which are not quoted on the Stock Exchange should if possible be avoided.

CHAPTER XIV.

BANKING PROFITS.

The Rate of Discount.

If a stranger to the great Metropolis visited the Bank of England on a certain day in the week, *viz.*, Thursday, he would witness a sight which might somewhat puzzle him. He might observe in one of the corridors, a crowd of persons, composed of telegraphic messengers, officials from various banks, discount houses and other kindred institutions, waiting patiently until a notice is displayed on the wall, stating that the rate of discount is so much per cent., or that no alteration has been made. Immediately this announcement takes place, the crowd quickly disappears. All this excitement would naturally puzzle a stranger, and he might ask a series of questions such as—What is the meaning of the term discount? Why should the Bank of England fix the rate? And again, What causes the rate to fluctuate?

We shall endeavour to answer some of these questions, which are of great importance to the mercantile world. These changes in the bank rate of discount are especially important to the banks of this country, because their profits or dividends are largely dependent upon the rate of interest. At every bank meeting reference is made by the chairman to the rate of interest ruling in the money market during the preceding six months, and what effect such rate has had upon the profits of that particular bank. The causes and effects of such changes are rather of a

complex character, because every year the English money market has to take note of new developments of trade and commerce.

As Prof. Marshall justly stated at a meeting of the British Association: "When economic problems become more complex every year, the necessity of studying them from many different points of view, and in many different connections, becomes more urgent".

The Bank of England, being, we might say, the most important storehouse of capital, has assumed the responsibility of fixing the price for the loan of capital. The variations in the amount of loanable capital existing in this country cause the price to fluctuate.

There are various forms of capital, but there is only one which concerns us—and that is floating or circulating capital. This kind of capital has been defined by J. S. Mill as that "which fulfils the whole of its office in the production in which it is engaged by a single use". Other kinds, such as houses, land, machinery, etc., it will not be necessary to consider, although the income derived from such property would increase the amount to be utilised as loans by those who can profit by its employment. Capital is said to be the result of saving, or a sacrifice of present enjoyment for the sake of the future.

The money income derived from the loan of capital is called interest, but we find the term discount used at the Bank of England. This word, however, in reality means the same as interest, because discount is the difference between a sum of money due at a future period and its present value, or a deduction that is made from the amount of a debt that is paid before it is due. The amount deducted depends upon the value of money or what we term interest.

There are other large houses grouped around the Bank

of England, and they collectively are known as the organised market for the loan of capital, or, in other words, the money market.

When we are standing inside the Bank of England we are, as it were, in the centre of the market.

The value of money, like every other commodity, is dependent upon the laws of supply and demand, but it differs from other commodities in being liable to great fluctuations.

Like the value of iron, tea or coal, the price for the loan of capital depends upon the state of the market.

In the money market, however, we do not ask the price of capital, but the rate of interest. Thus price and interest with regard to capital would be synonymous.

We will endeavour to state briefly some of the causes which affect the supply of capital. We have seen that the accumulations of capital are dependent upon self-denial. The people forego pleasures for the sake of future enjoyments. An increase of *surplus* income above the necessaries of life augments the *power* to save, and an increased regard for the future increases the *will* to save. Capital is originated by these means; and then we have people who become possessed of it and, not requiring the same for their own use, are so eager to lend it to others that they will accept a constantly lower and lower rate of interest.

We have therefore fluctuations of interest caused by an eagerness to lend.

Again, the accumulations of capital are dependent upon the rate of interest. If the rate is high, people save in order to obtain the advantage of a large return for their capital. If on the other hand the rate is low, the return is too small for the effort required to save.

The following formula shows how capital accumulates at

compound interest. Thus if I = rate of interest, then $\frac{69}{I}$ = the number of years for a sum of money to double itself. Thus if I = 5, then a sum of money would double itself in 13·8 years.

At the present time the growth of capital does not show any sign of overtaking the growth of the scope for its employment. It however happens that at stated periods there is a vast accumulation of capital, but in consequence of previous losses there is a want of confidence and consequently a dearth of new undertakings.

"In the market the rate of interest cannot fall beyond that limit at which it only offers just sufficient inducement to those who are on the margin of doubt whether to save or not. For if it did there would be a gradual shrinkage of capital relatively to the growing demand for it. Its marginal utility would rise in consequence of this relative scarcity, and therefore the rate of interest which is paid as the price of loans would rise also."

With regard to the demand for capital we find it is largely dependent upon the population, the natural resources of the country, and the state of trade. Thus the demand would vary with the prosperity of the country.

The commercial business transactions of this country are effected by means of borrowed capital. The trader enters one of the storehouses of capital designated a bank, and borrows capital for which he pays a certain rate of interest. With this capital he is able to purchase goods, and sell again at a profit after paying interest to the bank for the loan of the same. The trader's net profit would be the difference between the amount paid to the banker and the amount charged to the purchaser of his goods.

One of the reasons why the trade of this country has progressed so rapidly is due to the fact that capital can be

borrowed at a low rate of interest. We have given some elementary principles with regard to the laws of supply and demand in connection with capital, and have also stated that unlike other commodities it is subject to great fluctuations. Although we shall consider these fluctuations, yet it will be convenient to mention at this point why capital is subject to great changes. The great force at work which causes such changes, is the state of credit. The greater portion of the capital of the country finds its way into the banks, because the depositors trust such institutions with their surplus funds. The banks must find borrowers who require the loan of capital, or else it would lie idle and no profit would be made. This is especially the case when the banks allow interest on money deposited with them. The banks therefore act in the capacity of brokers. On the one hand they take capital from the depositors and lend it to others, *viz.*, the borrowers. We can easily understand that if at any time public confidence in such institutions becomes shaken, capital may be withdrawn from the banks by the depositors. These institutions in order to protect themselves from any sudden withdrawal of capital are obliged to keep in reserve a portion of their assets, which is called a reserve fund, to meet such contingencies. The tendency of the present day is for the banks to utilise capital as much as possible in order to avoid any waste, that is to say, to prevent capital from lying idle. This is of course beneficial in one way because it increases the profits of the banks, but on the other hand it makes our banking system a very delicate one. For example, in a speculative period there would be no capital available to meet a sudden demand. At such times traders exhaust their credit, that is, they have borrowed in excess of their means, and have greater liabilities than they can possibly

meet without the assistance of the banks. We should except, therefore, to see great fluctuations in the rate of interest when a speculative mania exists, because of a dearth of capital, created in some degree by small reserves held.

The state of credit is therefore of great importance in relation to capital. We have seen that a vast system of credit is founded upon the reserves of the banks, which are the great storehouses of capital. Therefore any increase or decrease in the proportion of such reserves must have a great influence upon the rate of interest.

The following remarks of Mr. Wynnard Hooper at a British Association meeting upon the London money market state clearly the present position of capital. He says:—

"The volume of business is larger and the liabilities of London and the whole country are much larger, but the reserve held against them is only slightly larger than was the case twenty years ago. The deposits of banks have enormously increased. Those of the fourteen principal London banks have risen from 103 millions in 1870 to 178 millions in 1889. Other banks' deposits have also increased, and a larger proportion of the deposits are kept in London to be lent. On the other hand, the reserve of the Bank of England is on the average very little larger than it was during 1870-9. Of course the reserve is now more efficient than it used to be for reasons already given, but nevertheless it is too small."

CHAPTER XV.

BANK OF ENGLAND RATE.

THERE were many reasons why the Bank of England became the great central organisation for determining the value of money or capital in the market. We have already seen that it possessed the exclusive right of joint-stock banking until the year 1826. In addition to this monopoly, the large capital at its command gave it a position above other institutions as a lender of money.

Besides its capital, the Bank had the privilege of issuing notes, which, of course, meant additional resources. In the year 1718 the note issue was £1,829,930, and has rapidly increased until the present year, when it amounted to £48,000,000. Thus from two sources, *viz.*, subscribed capital and note issue, the Bank of England became a formidable opponent to the other bankers. We can therefore understand how a single bank with large resources became a great power, and assumed the responsibility of fixing the rate, or the price for the loan of capital.

There was, however, another cause tending to give the Bank a predominant position, *viz.*, it became the custodian of the money belonging to the State. Again, when the Government required a loan it was called upon to carry out the transaction. At various times, therefore, it had large resources at its command. Our National Debt was built up by its aid, and thus from an early period the Bank and the Government have been allied.

In return for services rendered to the State, the Bank naturally looked to the Government for assistance during commercial crises and panics. The privileges bestowed upon it were therefore: 1st. The use of the Government balances, which at times are very large. For example, on the 9th January, 1895, the amount was £6,200,000. The community naturally thought that if the Government could trust the Bank, its savings would be quite secure. 2nd. It had, as we have seen, the monopoly of joint-stock banking until the year 1826. This gave it a good start before other joint-stock banks came into existence. 3rd. It was the only joint-stock bank in London which could issue notes. Thus from many singular events the Bank became the holder of the cash reserve.

There is rather a curious illustration showing the connection between the Bank and the Government. In the year 1797 Mr. Pitt, as Chancellor of the Exchequer, was afraid there would not be enough specie in the Bank to meet foreign payments, and therefore compelled it not to pay gold for notes issued. Naturally a bank which had the privilege of not paying cash for its notes must obviously assume a commanding position—in fact, it was an institution with a charmed existence. There are, however, two incidents in its history which materially assisted towards making it the principal dealer in capital, and in such capacity to state the price for its loans.

The first was in consequence of the London banks opening accounts at the Bank of England. These banks found it convenient to keep their reserves with that institution, because its premises were better protected, and also for the reason that the Bank issued notes, which could be retained far better than gold in their tills. Bank of England notes being a legal tender for payment of debts,

liabilities could be discharged, thus avoiding the use of gold to a large extent.

The balances of the London banks have at times been large. Thus in 1844 the amount was £1,000,000, but in 1872 the amount was £7,500,000.

In 1853 these balances never exceeded the reserve by 20 per cent., but in recent years the proportion has been 50 per cent.

	Proportion of Reserve to Liabilities	Proportion per cent. Bankers' Balances to Reserve.
Thus—1846-54 .	51 per cent.	22 per cent.
1855-63 .	43 ,,	48 ,,
1864-72 .	42 ,,	63 ,,

During the panic years of 1847, 1857, and 1866 the reserve of the Bank of England was insufficient to meet the bankers' balances.

		£
Thus—1857,	Bank's Reserve	1,462,153
	London Bankers' Balances .	4,649,000
1866,	Bank's Reserve	1,202,810
	London Bankers' Balances .	7,930,000

This additional capital which the Bank obtained from the London banks considerably augmented its resources, and any sudden withdrawal of these reserves must react upon the rate of discount, when such rate fluctuates with the amount of reserve.

The second incident in its history was that it assumed the position of a lender of capital to outsiders, that is, to those who did not keep a banking account with it. This is quite different from the practice of the English banks.

In times of panic and commercial crises a great number apply for loans at the Bank of England. The statistics given for the panic years of 1847, 1857, and 1866 show to what extent the community applied for assistance when needed. It has lent largely at various times, and therefore we find that during the present century the Bank has gradually assumed a responsibility over the money market

by rendering assistance to the commercial community. At such times all those who were possessed of good security were assisted by the Bank. The importance of this policy cannot be overrated, because, as we have seen, English trade is conducted by means of borrowed capital, and if the trader could not discount his bills he would soon be obliged to suspend payment.

The merchant purchases goods and pays for the same by means of bills drawn upon him, say three months hence, and he is only able to meet such bills by discounting others received for goods sold. It is therefore of vital importance that he should be able at all times to obtain capital by means of bills discounted. The Bank of England has therefore been of immense service to the commercial community at periods when capital is scarce or a feeling of distrust has pervaded the mercantile world. Its good management is therefore of the highest value. Thus when the deposits of other banks have diminished in consequence of a want of confidence on the part of the depositors, the deposits of the Bank of England have invariably increased.

With regard to the note circulation, the action of the Bank is purely mechanical; in fact, as Mr. Bagehot stated, the office could be removed to Somerset House.

The Bank is allowed to issue £16,800,000 of notes against securities, but for any amount issued in excess, the Bank must hold gold and silver in reserve. This limit was fixed by the Act of 1844, in order to secure the convertibility of the note.

The profit derived by the Bank from such issue is made from the securities which bear interest. The profit is, however, divided, the Government receiving £200,000.

The money market is affected when gold is taken from the Bank of England, and we shall see how it affects the

rate of interest when we consider the causes of the fluctuations. If, however, as Mr. Bagehot suggested, the department was removed to Somerset House, it is a question whether the loss of a million or two of gold would affect market rates like what takes place under the present conditions.

The weekly reports of the banking department are, however, of greater importance to the outer market, and these reports are keenly scrutinised in order to ascertain what are the forces which might affect the value of money.

We see in the daily papers an analysis in the following form:—

BANKING DEPARTMENT.

Last year. 10th Jan.	Liabilities.	2nd Jan., 1895.	9th Jan., 1895.	Increase.	Decrease.
£		£	£	£	£
3,428,491	Rest . .	3,192,427	3,383,624	191,197	...
4,899,202	Public deposits	6,598,906	6,213,105	...	385,801
31,360,264	Other do.	38,198,631	38,845,839	647,208	...
155,838	Seven day bills	143,967	147,618	3051	...
	Assets.			Decrease.	Increase.
11,760,317	Gov. securities	14,689,099	16,677,309	...	1,988,210
25,712,643	Other do.	24,026,528	21,305,245	2,720,283	...
14,893,580	Notes . .	21,731,120	22,914,375	...	1,183,255
2,018,455	Gold and silver	2,241,184	2,246,257	...	5,073
				3,562,339	3,562,339
46¾ %	Ratio . .	58⅜ %	55⅝ %	...	...
3 %	Bank rate .	2 %	2 %	...	...

ISSUE DEPARTMENT.

Last year. 10th Jan.	Liabilities.	2nd Jan., 1895.	9th Jan., 1895.	Increase.	Decrease.
£		£	£	£	£
23,795,585	Gold & bullion	30,849,895	31,633,855	783,960	...
40,245,535	Notes issued .	47,649,895	48,413,855	783,960	...
25,352,155	Circulation :	25,918,775	25,519,480	...	399,295

Those who study the figures very closely are able to guess

more or less accurately what has taken place during the preceding week. For example, if we take this particular week as an illustration, we note that the reserve in the banking department has decreased, which would show a greater demand for capital. We shall discuss in the next section the fluctuations of this reserve, and endeavour to understand how far the rate of interest is governed by its amount.

Although the Bank issues these weekly balance sheets, the directors do not state their reasons for making alterations. Sometimes an error of judgment occurs, but it is soon rectified, because the Bank cannot control the value of money. As the late Mr. Bonamy Price observed, "A banker is the interpreter of the forces at work, and he makes a trial of the rate which those forces prescribe".

In connection with the history of the Bank, we have already noticed a gradual growth of deposits, which shows that the public have great confidence in its management.

Although there has been a gradual growth of deposits, the Bank's position in the money market as a lender of capital has materially altered. Thus if we compare the total amount of capital lent by the banks of the United Kingdom with the amount lent by the Bank of England, we find the proportion is very small, *viz.*: In 1874 total lent by banks of the United Kingdom = £535,500,000; Bank of England = £10,800,000, or only 2 per cent. Again, its liabilities are small in comparison with the liabilities of the London joint-stock banks.

			£
Thus—1890,	Bank of England	. . . =	29,000,000
,,	11 London joint-stock banks	. =	125,589,000
1894,	17 Metropolitan joint-stock banks	=	231,800,000
,,	Bank of England	. . . =	44,600,000

Again, in 1854, the proportion of capital to the liabilities of the Bank of England was 14 per cent., but in 1874 the

proportion was reduced to 9 per cent. The Bank recognised the fact that its rate of interest was not always the market value, and consequently a few years ago informed the public that, although the minimum rate was published, yet under certain conditions it would discount bills below such rate.

Naturally this privilege would be granted to its own customers rather than to large financial houses which compete against it. The large borrowers of money in fact avoid the Bank if they can possibly do so, because it will only lend money for ten days, and sometimes charges 1 per cent. above the published rate.

In recent years the Bank has reduced the limit of loans from ten to seven days, but it reserves the right to state for what period the loan shall be made.

We have seen how the Bank gradually assumed a leading position in the money market, through its large paid-up capital, its large deposits, its being the bankers' bank, and finally by its holding the Government balances. There is, however, one important point in connection with its history, and that is, it assumed a great responsibility over the money market. In times of commercial crises and panics it undertook to lend capital to any one who was possessed of good security.

In 1825 the directors stated that the Bank had taken a firm and deliberate resolution to make common cause with the country. Mr. Hankey has said that the Bank ought never to have encouraged this opinion, but we cannot see how any other system could succeed when we consider its unique position. The only institution in this country which holds a gold reserve must of necessity be the final resource of the mercantile community.

During these periods of commercial disaster, the

amount of capital advanced by the Bank of England has been very large. The usual proportion of 30 to 50 per cent. of reserve against liabilities has not been kept, in fact the reserve at one time was so low as 6 per cent.

We will illustrate this policy on the part of the Bank by giving the amounts advanced during the great crises of the present century. With an increased demand for capital, the Bank at such periods naturally charged a high rate of interest, *viz.*, from 6 to 10 per cent.

BILLS DISCOUNTED BY BANK OF ENGLAND.

	£		Rate.
1809	15,475,700		
1810	20,070,600	panic year.	
1825, Feb. 28	2,466,000		
,, Aug. 31	5,486,000		
1826, Feb. 28	9,597,000	crisis year.	
,, Aug. 31	2,950,000		
1836, Feb. 20	2,900,000		
,, Aug. 30	4,400,000		
1837, Feb. 28	11,200,000	crisis year.	4½ to 5 per cent.
,, Aug. 29	5,100,000		
1838, Feb. 27	3,200,000		
,, Aug. 29	2,900,000		
1846, Feb. 28	13,137,000		3 per cent.
,, Aug. 29	6,067,000		4 ,,
1847, Feb. 27	8,879,000		5½ ,,
,, Aug. 28	9,163,000		5 ,,
,, Oct. 2	10,399,000		5 ,,
,, ,, 9	10,978,000	crisis year.	5½ ,,
,, ,, 15	11,907,000		
,, ,, 23	12,492,000		8 ,,
1856, Feb. 23	8,883,000		5½ to 4½ ,,
Aug. 30	4,446,000		6 ,,
1857, Feb. 28	8,859,000		5½ ,,
,, Aug. 29	7,893,000		8 ,,
,, Oct. 24	9,636,000		
,, ,, 31	11,105,000		
,, Nov. 4	11,439,000	crisis year.	10 ,,
,, ,, 11	13,233,000		
,, ,, 18	16,003,000		
,, ,, 25	17,376,000		
,, Dec. 2	17,788,000		

In 1857 the Bank stated that advances would only be made to bill brokers at certain seasons when the public deposits were particularly large, but at other times an application for an advance would be considered exceptional. The Bank, however, in the panic year of 1866, disregarded this rule.

BILLS DISCOUNTED.

	£	Rate.
1866, Feb. 28	7,253,000	7 per cent.
" May 2	8,834,000	6 "
" " 9	9,249,000	7 and 8 "
" " 16	13,831,000	9 and 10 "
" " 23	14,501,000	10 "
" " 30	16,512,000	10 "
" June 6	16,003,000	10 "

The policy of the Bank during the critical years of 1872-3 and 1878-9 has been ably defended by Mr. Birch, the late governor. He says: "In 1872-3 an enormous amount of bills were created with a view of withdrawing gold from England to assist in the payment of the French indemnity to Germany. The Bank recognised the danger which might arise from this being carried to too great an extent, and then crippling the ordinary business of the country, and rapidly raised the rate of discount. I find that in 1872 we had seventeen changes in our rates of discount; in 1873 we had twenty-four changes. The bank rate varied from 3 per cent. to 9 per cent., and from 10 per cent. to 12 per cent. was charged in the latter period on advances, not with a view of making large profits, but with a view of telling people that it was a class of business the Bank would do everything in its power to keep within reasonable bounds."

In October, 1878, came the crash of the failure of the City of Glasgow Bank. The Bank of England was in a good position to meet the emergency, and the threatened crisis passed away. The rate was never raised above

6 per cent.: many thought it should have gone higher, following the precedents of 1872-3, but in doing so they did not recognise the fact that the circumstances connected with these periods were entirely different.

"In the year 1873 the stringent action on the part of the Bank was with a view to put a stop to the discounting of certain financial bills, and in the year 1878 the main object of the Bank was to avoid all unnecessary cause for alarm; and, the foreign exchanges being in favour of this country, the Bank could show a bold front to the difficulties of the situation, and did so, and I venture to think its action met with general approbation."

This is a very important declaration on the part of the governor of the Bank, showing that its present policy is to assist the money market within reasonable limits. In the year 1890 the directors even went a step further in order to prevent a great disaster. When the great house of Baring was in difficulties, the directors called a meeting of the representatives of the principal banks, and agreed with them to guarantee all the outstanding acceptances of the above-mentioned firm. This action on the part of the Bank no doubt prevented a great commercial disaster. We think the policy was possibly wise under the circumstances, but whether the Bank of England should guarantee the solvency of houses of repute when in difficulties is a question for serious consideration. A crisis might have been avoided in 1866 when the house of Overend, Gurney & Co. failed, but when a bad system of finance exists it is better that firms who embark in reckless speculation should not be assisted. Of course this is a different policy from that of refusing to assist the market when it may be the means of avoiding a panic.

The Bank has recently made concessions to its rivals in the money market, *viz.*, the bill brokers. The Bank has agreed to discount bills for them which have not more than fifteen days to run at not less than bank rate, but of course it reserves the right to charge a higher rate. No doubt this will tend to make the Bank of England rate more in harmony with that of the outer market.

The position of the Bank of England is unique, in fact no country has an institution wielding such power over the supply and demand of capital.

It is satisfactory to observe that the great powers entrusted to the Bank have not been abused. To promote the prosperity of the country has been its aim rather than to pay high dividends to the stockholders.

CHAPTER XVI.

CAUSES OF FLUCTUATIONS OF RATE.

WE will now consider the causes of fluctuations in the bank rate. They are of a varied character, in fact each year brings to light some new force which affects the value of money.

The first great cause would be the state of English commerce. The trade of this country is, as we have seen, transacted by means of borrowed capital obtained from the banks, which are the great storehouses of capital.

When trade is active more capital is required, and therefore we should expect the rate of interest to rise. On the other hand, when trade is depressed less capital is necessary for the requirements of the country.

Our imports and exports are a good index as to the state of trade. Every month we see reference made in the money articles of the daily papers, as to the increase or decrease of our commerce. The reports from our consuls abroad, also inform us whether capital is required in various parts of the world.

When trade is active we should expect prices to rise because of an increased demand. When this occurs we get merchants anxious to take advantage of the improvement in commerce, and therefore increase their business by means of borrowed capital.

Again, when prices are rising, the merchant is able to borrow more capital from the banker, because of the increased value of his goods. We should also expect to

notice the imports increasing with a rise of prices, because other nations are anxious to send goods to this country in order to obtain higher values for their commodities.

On the other hand, exports would be diminished because the rise of prices would cause a less number of purchases to be made in this country for export, in consequence of the margin of profit becoming less on each transaction. Whenever there is a *great* difference between the values of imports and exports, the balance finally must be paid in gold, the only commodity which can be utilised for settling international indebtedness. Of course, one notices a great discrepancy between the values of our imports and exports, and therefore one would imagine that large sums of gold have continually to be sent from this country. This, however, is not the case, because England has lent enormous sums to foreign countries, which have to remit money as interest.

Again, this country derives a large income from her carrying trade. When, however, there is no equilibrium the balance must be paid in gold, and that metal can only be obtained in large quantities from the Bank of England. This is one of the reasons why the reserve of gold at the Bank is so important. As gold represents capital, its movements to and from this country show to some extent the supply and demand for capital.

Another important cause is that the reserve of gold in the vaults of the Bank represents the final resources of this country for meeting cash payments. We have seen that the banks keep their reserves at the Bank of England, and consequently there is no other stock of gold in existence. All sudden demands must be met by that institution.

Our credit system is so vast that one naturally looks to the stability of the banks which hold the surplus capital

of the country. If the banks were called upon to repay all their depositors at a given time, they would be unable to do so. The state of credit is therefore an important item in studying changes in the rate of interest.

All sudden demands for capital soon affect the reserve at the Bank of England. As we recognise in this country the importance of keeping a reserve for emergencies, it is important that something should be done to protect such reserve. Fortunately the Bank of England has a good instrument to protect its resources, *viz.*, the rate of discount. Capital soon finds its way to the centre where the highest rate of interest prevails. The reserve at the Bank is therefore of great importance, and consequently it is necessary to understand how it influences the value of money. There are in reality three aspects of the reserve.

In the first place, the currency requirements of the country are obtained from the Bank. We shall have a good illustration of this, when we consider the autumnal demand for gold.

Secondly, a greater part of the bullion which is required for international purposes is obtained from the amount deposited.

Finally, there is the reserve of gold and notes in the banking department, which is of the greatest importance in influencing the rate of discount.

The daily papers continually make reference to the reserve in commenting upon the value of money. To an outsider not conversant with the familiar terms used daily in Lombard Street, the remarks sometimes made are misleading. We find reference made to the reserve of gold and notes in the banking department, and then, possibly in the same paragraph, reference to the bullion in the issue department. We are then informed that although a fair reserve exists in the banking department

yet we must expect to see capital very dear, because a million or two has been drawn from the issue department.

By the Act of 1844 the Bank is allowed to issue fifteen millions of notes against securities, and for any sum issued in excess gold must be held in reserve.

It is clear that any one holding notes can obtain gold from the Bank, because that institution is compelled to pay in coin all notes presented for that purpose. How then does the withdrawal of gold from the issue department affect the value of money?

Mr. Clare, in his excellent book entitled *A Money Market Primer*, shows the effect of a withdrawal of gold on the reserve at the Bank of England.

Thus, when a depositor withdraws £500,000, notes to that amount are taken from the reserve and returned to the issue department. These notes are cancelled, and sovereigns which are held against them are given in exchange. The effect on the balance sheet is as follows:—

ISSUE DEPARTMENT.

Notes . . .	£38·8 millions	Securities . . .	£16·4 millions
		Gold	22·4
			£38·8

Withdrawal.

Notes . . .	£38·3 millions	Securities . . .	£16·4 millions
		Gold	21·9 ,,
			£38·3

BANKING DEPARTMENT.

Capital and Rest	£18 millions	Government Securities	£11·7 millions
Deposits . .	37·2 ,,	Other ,,	28·7 ,,
		Notes	13·8 ,,
		Coin	1 ,,
	£55·2		£55·2

Withdrawal.

Capital . .	£18 millions	Government Securities	£11·7 millions
Deposits . .	36·7 ,,	Other ,,	28·7 ,,
		Reserve . . .	14·3 ,,
	£54·7		£54·7

If, however, the money market restores its balances to the former level, it borrows of the Bank of England or discounts bills at that institution.

We have already seen that gold is the final means for settling international trade, and that it can only be obtained in large quantities from the Bank of England.

When capital is leaving this country in the shape of gold it represents a variety of transactions—such as a scarcity of capital at a foreign centre, or to pay for food imported into this country, or possibly to carry out a large financial operation.

In addition to the currency requirements of this country, it is necessary to keep a certain amount of gold in order to preserve the convertibility of bank notes.

We are informed sometimes that the Bank directors have decided to raise the rate, because possibly a small quantity of gold has left the Bank; whereas the actual cause might be a depletion of the reserve in the banking department, caused by a scarcity of capital, or possibly other considerations known only to the Bank directors. Of the two reserves of which we have spoken, it is certainly the reserve in the banking department which is most important in causing fluctuations in the rate of discount.

Mr. Palgrave says: "Though the total amount of bullion held by the Bank is a very important thing, the rate of discount does not appear to be regulated by it".

This is shown by the following returns:—

		£	Rate of Discount.
1844	Bullion held	13,500,000	2½
1845	,,	15,200,000	3
1846	,,	14,800,000	3½
1854	,,	17,500,000	3⅝
1856	,,	10,900,000	5¾
1857	,,	10,100,000	6¾
1858	,,	17,800,000	3¼

		£	Rate of Discount.
1865	Bullion held	14,500,000	4¾
1866	,,	14,900,000	7
1870	,,	20,400,000	3
1871	,,	23,500,000	3
1872	,,	22,600,000	4¼

We know that at times the market suffers from a scarcity of capital rather than of gold. The figures which we have given show that on several occasions the reserve of gold in the issue department has been low, and yet the rate of interest has also been low; but there is a closer connection between the reserve in the banking department and the rate of discount.

It has been already stated that the demand for capital does affect the amount of bullion in the issue department. Capital is required to pay for the balance of trade against us, and must be liquidated by means of gold drawn from this department. It indicates that capital is leaving this country for the payment of food and other necessaries purchased. The all-important question is, How much gold should be retained in the issue department to meet every contingency?

There is no doubt that the Bank is able to attract bullion from abroad when its reserves of that commodity are low by raising the rate.

On the other hand we must remember that the Bank has not experienced in the last fifty years a run on its resources for gold. So long as notes can be obtained, the holders do not appear to require gold in exchange. In consequence of the banks keeping their reserves at the Bank, they retain in their tills a less amount of gold; although the liabilities of the banks have increased, yet the amount of cash held is smaller.

			Cash held.
Thus—1890,	11 banks' liabilities,	£161,326,100	10·3 per cent.
1879	,, ,,	125,539,000	12·8 ,,

Of course, improved communication, the use of telegraphic transfers, and the great use of cheques have economised gold. Yet, on the other hand, a sudden demand for that metal must be met by the Bank of England. We therefore get changes in the rate of discount, due to the movements of comparatively small amounts of gold.

Mr. Giffen estimates that with a capital of 6000 millions the quantity of gold and silver held only amounts to 20 millions, or 3 per cent.

Any increase or decrease in the amount must affect the value of money, and these changes are reflected in the reserve of the Bank of England. All transactions are expressed in gold, and therefore if we get prices rising an additional amount must be added to the nominal capital, and particularly to the capital represented by the loans and deposit of banks. If wages rise in this country more gold is required, and consequently the reserve at the Bank is diminished.

Our monetary system is a delicate one, and what M. de Laveleye stated in 1864 is possibly of more force at the present time. "All countries which carry on gigantic transactions with small reserves of gold and silver, and which have a vast movement of importations and exportations, must be exposed to these economical perturbations. The more a country expels the precious metals from the channels of circulation and replaces them by instruments of credit, bank notes, cheques, warrants, deposits, clearing houses, etc., and the more, at the same time, it develops its relations with foreign countries, the more it will be exposed to the periodical return of financial perturbations, because more easily an unfavourable balance of trade and payments will disturb all the mechanism of exchange, and will require from the managers of credit institutions redoubled circumspection, prudence, and ability."

We have in this country a gigantic system of credit built up on a small gold reserve, and in order to protect the same the Bank of England has very frequently to alter the rate of discount.

By raising the rate capital is attracted from abroad, and the reserve at the Bank is replenished.

London being the financial centre of the world, all foreign countries naturally ascertain the rates of interest prevailing in London, and if higher rates are ruling here capital finds its way to the most profitable market.

The effect of high rates prevailing in London soon makes itself felt on the trade of this country. Prices of commodities would fall, and this would tend to diminish imports; but, on the other hand, exports would be increased, and would have to be paid for by means of gold.

If we study the Bank reports we shall observe that the rate of interest is dependent upon the reserve, principally that of the banking department. With a low reserve the rates of interest are high, and with a high reserve a low rate of interest. This is shown from the following table:—

	Reserve.	Rate of Discount
1845-49 . . .	8·5 millions	£3 11 4
1850-54 . . .	9·8 ,,	3 5 10
1855-59 . . .	8·5 ,,	4 14 3
1860-64 . . .	8·4 ,,	4 15 2
1865-69 . . .	9·6 ,,	3 18 8
1870-74 . . .	12·3 ,,	3 10 3
1875-79 . . .	13·8 ,,	2 19 7
1880-84 . . .	13·4 ,,	3 7 7
1885-91 . . .	13·7 ,,	3 8 4

Fluctuations in the rate of discount are therefore due to the movements of comparatively small amounts of capital. We have, as it were, all the forces which affect the money market concentrated upon the reserve of the Bank of England.

Mr. Giffen says that "the rate of discount in the

short loan market of a banking centre like London is not to be identified with the rates for loans generally, and it is only the rate for special loans between special classes of borrowers and lenders. Every change tells on the *sensitive* short loan market."

The position of the Bank of England in the money market is that of a large dealer who fixes the price, and then sees whether customers will transact business. Outside the Bank are grouped large dealers in capital, who undersell the Bank in order to get business.

These large money dealers are known as bill brokers, who obtain their principal resources from the banks and then discount bills at low rates in the market. It seems rather an anomaly that the banks should lend capital to outsiders to enable them to discount bills at fine rates. The effect of this has been that the banks get a less number of bills for discount than formerly. This change in the system of banking business is to be regretted, because good bills are one of the best investments for surplus capital.

A few years ago the bill brokers only discounted the acceptances of large financial houses and those of the various banks, but at the present time they discount a large amount of trade bills.

Bankers, however, find it convenient to lend their day to day balances to the broker, because an investment is at once found for surplus resources, and the money so lent can be called in at a day's notice. It must also be remembered that banks allow interest for deposits, and therefore it is necessary that no portion of the capital entrusted to them should remain unproductive.

The bill brokers either lodge bills which they have discounted as security for money advanced at call or short notice or they deposit marketable securities such

as Consol Certificates, India Government Bonds or Indian Railway Debentures. The latter class of securities are known as "floaters". When the loan is called in, the banker returns such hypothecated securities.

As the bills which are lodged as security mature, they are replaced by others having a longer time to run.

The position of the bill brokers is however one of great delicacy, because they are dependent upon the banks for the greater portion of their funds. If the banks have no surplus capital to lend, the brokers apply at the Bank of England for loans, in order to meet their requirements. However, they always endeavour to avoid making applications at the Bank because that institution only grants loans for seven days, and it is manifest that within a week great fluctuations might occur in the value of money.

No doubt this system of lending capital to the bill brokers has an important effect upon the value of money. This is shown in the daily quotations for money. We find sometimes the bank rates say 5 per cent., whilst the market rate is only 3 per cent. If the Bank finds its discount business getting less, it lowers the rate in order to bring it more in conformity with the market. The Bank certainly does affect the rate for money at a particular moment, but it cannot affect the average rate.

"The reason is that any momentary fall caused by the caprice of such a bank tends to create an immediate rise, so that upon an average the value is not altered."

There is therefore no ground for believing that the price of capital is governed by different laws than that of supply and demand like any other commodity.

We have already stated that both the demands for the internal and foreign trade of this country are reflected in the reserve of the Bank of England. With regard to the

foreign trade, we are able to understand the position of the market by the foreign exchanges. These tell us whether a demand for capital exists in any of the great financial centres of the world. All the forces which affect the supply and demand for capital are exhibited in these rates.

The following table shows us the extreme points when gold is likely to reach this country or the reverse :—

Paris	25·32½ = 4 per mille for us.
,, ...	25·22½ = par of exchange.
,, ...	25·12½ = 4 per mille against us.
Berlin	20·52 = 5 per mille for us.
,, ...	20·43 = par.
,, ...	20·33 = 5 per mille against us.
New York	4·89 = 5 per mille for us.
,, ...	4·867 = par.
,, ...	4·827 = 8 per mille against us.

The par of exchange is the identical value of the sovereign expressed in its foreign equivalent.

The extreme fluctuations of the exchange are known as bullion points, because when the rates reach these points, gold would be shipped either to or from this country. However, it is possible for the rates to rise or fall beyond such points, because on the shipment of gold to and from this country a saving might be made on freight, insurance, and other charges. One mercantile house might be in a better position than another to secure better terms on the shipment of gold.

Our trade is continually shifting from one place to another. A fresh demand for capital springs up in one corner of the globe, followed possibly by a diminished use of it in another. All these movements of capital react upon the price of commodities and in their turn affect the foreign exchanges.

Many years ago the Bank directors looked to the foreign exchanges as their principal guide in fixing the rate of

discount, but in recent years they have considered the demands for capital by the Stock Exchange as being of more importance.

Mr. Birch says: "The great thing which governs us is the enormous transactions on the Stock Exchange in France, in Germany, and in the United States. These are the operations we have to follow most carefully."

All such demands would affect the reserve of the Bank of England. The following figures will give us some idea of the demand for capital by the Stock Exchange:—

In 1889 there were registered 2788 companies with a capital of £241,277,000, the largest number ever registered, exceeding the previous year by 238.

Of course all these companies were not floated. Since the Companies Acts were passed 33,901 companies have been registered with a capital of £3,740,520,000. The year 1895 gave the following stupendous figures: 18,362 companies in existence with a capital of £1,035,029,835.

Mr. Giffen has estimated the capital of the country to be £10,000,000,000, and we observe that the figures for 1889 are very large, *viz.*, about one-fortieth of the total amount. Although it does not represent capital paid up, yet the amount is very large.

Some of this capital would be sunk in railways, mines, docks and kindred undertakings, and would not be reproduced for a long term of years.

When there is a great increase in the number of joint-stock companies, it may happen that the savings of the country are not sufficient to meet the great demand, and then the value of money must be high. Shareholders are unable to pay their calls without the assistance of banks, and consequently the rate of interest rises.

Besides the fluctuations due to the increased demand

for capital in order to meet the requirements of trade, there are changes which occur annually.

Of these periodical changes, the most important is the autumnal demand, which is principally a currency requirement.

The cause of this demand is, that after the ingathering of the harvest a great number of transactions take place. Corn is sold and other commodities are purchased. All this tends to an absorption of capital.

The weekly returns of the Bank of England for the third and fourth quarters of the year show the result of these transactions, in a marked decrease in the bullion and loanable capital.

There is also the autumnal demand for gold from Scotland, due to the fact that rents, salaries, etc., are paid on the Scotch quarter day, *viz.*, 11th November.

At this period of the year the Scotch banks exceed their authorised issue of notes and are therefore obliged by the Act of 1845 to hold gold in reserve against any excess. After the demand has subsided, this hypothecated gold soon finds its way back to the Bank of England.

Professor Jevons speaks of the autumnal demand as follows: "To sum up, then, the October drain is due like many others to economic disturbances, to a concurrent of causes. The dispersion of money in wages during the summer and the absorption of money and capital in buying up the produce of the harvest occasion a general autumnal drain upon the resources of the banks, causing the private deposits, the bullion and the reserve of notes to fall. Then the general quarterly payment of rents, bills, and especially the dividends at the beginning of October, cause a sudden extra run upon the resources of the banks quite sufficient in many states of the money market to engender a panic, unless indeed its normal and

temporary nature be well understood. The result of this autumnal demand is that we find the value of money higher for the last six months of the year."

This is shown by the following analysis of bank rates :—

		Average rates.
1845-61	January to March	3·97 per cent.
,,	April to June	3·87 ,,
,,	July to September	3·60 ,,
,,	October to December	4·17 ,,

The Bank of England pays the interest on the National Debt by quarterly instalments on 5th January, 5th April, 5th July and 5th October. The effect of these payments is shown in the weekly balance sheets :—

(1) A rapid decrease in Government deposits.

(2) A decrease in the reserve of notes.

(3) A decrease in the private securities.

(4) A slight decrease in the bullion.

(5) An increase in the private deposits.

(6) An increase in the note circulation.

When the dividend money, now about £5,250,000 per quarter, is released, it has the effect of increasing the supply of capital, and consequently at these periods we may expect the rate of interest to fall.

The financial requirements of the Chancellor of the Exchequer frequently cause changes in the value of money. This is especially the case when there is a large sum floating in the market in the form of Treasury or Exchequer bills. The repayment or renewal of such obligations has an effect upon the value of money, especially at times when capital is scarce. The rates at which these obligations are renewed, would be an indication to the Bank directors as to the position of the outside market.

In the financial papers reference is made to certain payments or calls which fall due. For example, an instalment on an Indian loan of say £1,000,000 has to

be paid, and consequently the market is denuded of that amount of capital. Again a large company makes a call upon its shareholders, who are obliged to find capital to meet the same. Then at the same time we might have the Government borrowing £1,000,000 on Treasury bills. These bills are issued at various dates, and if they are applied for at low rates, it would indicate that the market expects a low average rate for money.

The effect of all these calls upon the market would be to raise the rate of interest.

We often see it stated that the Bank of England has been borrowing on stock. This means that it borrows capital in the market, like the bill brokers. The weekly reports show this by a decrease in Government securities. The Bank directors endeavour to make their rate more effective, or, as it is stated, to get control of the market.

It is difficult to understand how capital so obtained by the Bank can be utilised at a profit, but when the Bank gets control of the market, it is able to get more discount business; which no doubt would more than compensate it for the amount paid as interest on loans.

The rates for money prevailing on the Stock Exchange form a guide to the Bank directors in fixing their rate. They study closely the events which are taking place in the great market for securities.

A large portion of the business transacted on the Stock Exchange is of a speculative nature. Stock is purchased, but not paid for, so that when the fortnightly settlement arrives, the buyer has to obtain a loan on his stock, or, as it is termed, "carried over" to the next settlement. This is done by the broker, who charges his client interest for the transaction. The rate of interest charged affords some indication as to the scarcity of capital or otherwise.

We have been considering some forces or economic causes which tend to increase the value of capital in the market. There are, however, causes which have the effect of lowering the rate of interest.

Sometimes a large Government loan is paid off, which has the effect of throwing capital on the market. Again, a railway is purchased by a Government and its capital returned to its shareholders. This recently occurred, when a Dutch railway was purchased by the Government, and produced some effect upon market rates. We have, in fact, rates for money continually changing in consequence of the movement of comparatively small amounts of capital.

However, for more permanent causes of annual average rates, whether high or low, the condition of trade is the most important factor. When trade is depressed, less capital is required, and therefore years of depression would mean low average rates of interest.

Our commercial system is highly organised. The division of labour has made trades dependent upon each other. A depression in one trade soon affects another, and this reacts upon the banks, which find that less capital is required, and consequently rates for money fall.

Again, we find credit an important factor in the money market, not only in connection with the mercantile community, but also with banks. Trade is carried on by means of borrowed capital obtained from the banks, which lend capital belonging to others.

A greater portion of the resources of banks is utilised in the discounting of bills which represent credit transactions, and we have seen that the term discount is used in the money market rather than the term interest, showing that the purchase of these credit documents is the most important business in the money market.

We have already stated that the Bank is only in the position of one of the largest dealers in capital. We must, therefore, consider the action of the other lenders, especially the bill brokers and large discount houses, that wield a great power in the market. These institutions compete against the Bank, in order to obtain capital and to utilise the same in the discount of bills.

For example, the effect of this competition may be seen by the following quotation of rates prevailing at one time in the market, *viz.* :—

Discount.	Per cent.		Money.	Per cent.	
Bank rate . . .	5	...	7 day Bank of England loans . . .	6	...
3 month bank bills .	$4\frac{5}{8}$	$4\frac{3}{4}$	Bankers' deposit rate .	$3\frac{1}{2}$	...
6 ,, ,, .	$4\frac{1}{2}$	$4\frac{3}{4}$	Brokers' deposit rate .	$3\frac{1}{2}$	$3\frac{3}{4}$
3 month fine trade bills	5	...	7 day market loans .	$3\frac{1}{2}$	4
6 ,, ,,	5	...	Day to day money . .	$2\frac{1}{2}$	3

The above rates tell us somewhat as to the position of the money market.

We note that the rate for three month bank bills differs only $\frac{1}{4}$ per cent. from the bank rate. This would indicate that the Bank is able to effect some discount business, and, therefore, that its rate conforms to the market value for capital.

The rate for six month bank bills is a fraction less, because the market assumes that the average value of money for that period will be less.

It is to be noticed that the rate for fine trade bills is a little more, *viz.*, from $\frac{1}{4}$ to $\frac{1}{2}$ per cent. This additional interest is charged because more risk attends the discount of trade bills than bills accepted by banks, which will almost to a certainty be paid.

We observe that the Bank charges 1 per cent. above the published rate for seven day loans. This is the usual custom of that institution, and therefore every dealer in

money endeavours to meet his engagements without its aid.

The banks generally allow $1\frac{1}{2}$ per cent. below bank rate for deposits, unless the rate is very low, when there is only a difference of 1 per cent. Recently, we have seen the rate for deposits allowed by the banks lowered to $\frac{1}{2}$ per cent.; whilst the Bank of England remains at the nominal rate of 2 per cent. This would show the great difficulty experienced in utilising deposits at a profit. The cause of this difference between discount and deposit rates is that the banks have at times to lend money at call, at rates much below bank rate. Then again, they have to find an investment for depositors' money, which of necessity entails risk, and, therefore, some margin is required as an insurance fund. We note that day to day money is only worth $2\frac{1}{2}$ to $3\frac{1}{2}$ per cent., and, therefore, if a banker allowed $3\frac{1}{2}$ per cent. on deposit, there would be a loss by the transaction. However, it is the *average* rate which must be considered.

The brokers' deposit rate is a little higher than the banks', *viz.*, $\frac{1}{4}$ per cent., which would indicate that they are anxious to secure the use of capital, and therefore are willing to pay a higher rate.

The brokers prefer a low average rate for money in order to conduct their business rather than a rate continually fluctuating. The profit of the brokers would be the difference between their deposit rates and market rates for discount. They also allow an additional $\frac{1}{2}$ per cent. for money lent them for seven days, in order to avoid applications to the Bank of England.

The last quotation is for day to day money, that is, money which can be called in at any moment by the banks. Naturally money borrowed on such conditions is not so valuable to the broker, because, if loans are called

in, he is obliged to borrow elsewhere, and what the requirements of the market will be on the following day, may not be known.

By studying these rates we get an insight into some of the forces which cause fluctuations in the value of money. The tendency in the money market is towards an equalisation of rates. Naturally every borrower endeavours to find the cheapest market. When bills of a certain class are discounted at the banks, it is in consequence of the holders not being able to discount them below bank rate, because, although their credit is good, yet they are not sufficiently known in the market. The forces at work in the market are always tending to make the bank rate equal to the market rate. When there is a great discrepancy between the two, a less number of bills are discounted at the banks. Some of the large banks, however, compete for bills, that is, they discount for their customers at market rates, and such banks would not experience the movements indicated.

Again, the London banks soon ascertain how rates of interest are tending by the daily applications of the brokers. When capital is scarce in the market, the bill brokers visit the banks perhaps two or three times a day in order to obtain the surplus capital of such institutions, and offer at times even higher rates than the bank rate, in order to avoid applying at the Bank of England for loans.

CHAPTER XVII.

EFFECT OF CHANGES IN RATE.

Having briefly considered the cause of changes in the rate of discount, we will now study some of the effects. Of these the most important would be in relation to the commerce of this country, because, as we have seen, the greater part of our trade is carried on by means of borrowed capital.

Every change in the price of money must of necessity react upon the value of commodities. Merchants purchase goods on the presumption of being able to borrow capital at all times. If borrowing becomes difficult or disorganised, the whole trade of the country suffers. Of course, profits made on the purchase or sale of goods are considerably affected by the fluctuations in the rate. If a merchant has to pay a higher rate for the loan of capital than he has estimated in a contract, his profit might be reduced to nothing.

Trade would become restricted if they were abnormally high, because merchants would find it difficult to obtain a correspondingly higher value for their commodities.

If, however, we get low rates of interest, production would be stimulated, and, as a consequence, trade would be active, but a high rate of interest does not materially affect commerce, although great fluctuations may be detrimental.

A high rate would stop speculation, and this at times is beneficial to the country. It would be the means of

preventing a certain amount of circulating capital being converted into fixed, that is, expended in the construction of railways, mines, docks, and other similar undertakings. In such cases capital would not be reproduced for a long term of years.

We find reference made in financial journals as to the price of capital in relation to trade. They inform us that at times the rate of discount should be reduced in order to afford relief to the mercantile community. This demonstrates how closely the trade of this country is associated with the value of money.

Mr. Bagehot has stated that "Lombard Street is by far the greatest combination of economical power and economical delicacy that the world has ever seen". It is the centre or the money market of the whole world. All demands for capital are supplied from this centre.

If a foreign Government wishes to borrow capital, the rate of interest prevailing in Lombard Street would first be ascertained. If the rate was high, the Government would wait for a more favourable opportunity. Every nation wishes to borrow cheaply, and therefore avoids a market where money is dear.

The English market has been invariably a cheap one for borrowers, and therefore foreign States have found it advantageous to borrow here, rather than in Paris, Berlin, or New York.

This is seen from the average rates since 1845:—

1845-54	£3	8	8
1855-64	4	14	8
1865-74	3	16	5
1875-84	3	3	8
1885-94	3	3	2

The rate of interest allowed by the banks for money on deposit is determined by the bank rate. The London banks generally allow 1½ per cent. below bank rate unless

the rate is very low, when there is only a difference of 1 per cent. We have explained elsewhere the reason of this difference. The London banks and discount houses announce in the daily papers their deposit rates the day after the bank rate is fixed.

If a high rate of interest is allowed, we should expect to see the deposits in banks increase, but if low the deposits would tend to decrease, because the depositors would naturally find other investments for their capital. It may, however, happen in consequence of the difficulty of finding employment for capital, and also in consequence of a want of confidence, the deposits in banks may increase, although the rate allowed is only ½ per cent.

The value of money in the London market soon affects the rates prevailing in other great commercial centres, such as Paris, Berlin, Vienna, Amsterdam, and New York. The changes in the bank rate are soon reflected in the foreign exchanges. Thus, with a high rate prevailing in the London market, we should observe that the exchanges would gradually tend in favour of this country. This is in consequence of capital being sent here for investment.

We might say that London is the great clearing house of the world. More bills of exchange are drawn upon London than any other commercial centre, and such bills are a favourite investment on the Continent. The holders of such bills profit by the variation in the rates of exchange.

Mr. Goschen refers to this subject in his book on the foreign exchanges, thus: "We now come to the fact which it is very important clearly to appreciate, that at any moment there is in the hands of bankers and exchange dealers a large amount of bills on foreign countries, held partly for the purpose of speculating on a rise or fall in the price of bills, but to a very large

extent solely for the sake of the interest which is to be made on them. Bills on England, owing to the high rate of interest which they often bear as compared with continental rates, are a favourite investment abroad. In Paris, Berlin, Frankfort, Hamburg, and other continental cities, the bills on England held by bankers and joint-stock companies often amount to many millions sterling, and a very large sum remains in their hands for several months, in fact from the time when the bills are drawn to the time when they fall due."

The changes in the rate of discount have a considerable effect on the Stock Exchange, where vast amounts of capital are lent fortnightly, and consequently such changes soon affect the value of securities. If rates are low, speculation increases and more purchases are effected. Various stocks are bought because the rates of interest on such stocks are higher than the rate which the borrowers pay to the banks.

Supposing £10,000 Colonial Stock is purchased and the stock bears 4 per cent. interest, and $2\frac{1}{2}$ per cent. is paid for the loan of capital advanced on it, then the purchaser gets $1\frac{1}{2}$ per cent. by the transaction if he is able to borrow from one settlement to another.

Again, a low rate encourages speculation, because, the brokers being able to borrow cheaply, there is a tendency for all securities to rise.

The rates charged for "carrying over" stock on the Exchange fluctuate with the bank rate of discount, and if such rates are high, speculation is checked and the price of securities falls. There is therefore a close connection between the rates for money and the price of securities.

We will briefly consider the effect upon some of the securities dealt in on the Stock Exchange. At the

head of such securities would be British Government Funds, which are particularly sensitive to changes in the rate of interest. They form a floating security in the money market. The large financial houses are able to borrow capital from the banks against Consols, and, if the average rate of interest in the market is higher than the rate on Consols, there would be a tendency for the price to fall. The holders would prefer selling their stock and lending capital in the open market.

If, again, the banks offer a high rate of interest for deposits, the holders of Government Stock might prefer selling to get the higher rate. With a high market rate prevailing the banks would be inclined to sell Government Stock in order to lend the proceeds to bill brokers, and thus secure a more remunerative return for their capital.

Again, the price of Treasury and Exchequer Bills is largely affected by the market rates for money. These securities like Consols are utilised by discount houses as cover for advances made by banks to such institutions. We therefore find the price of these securities fluctuating with the market value for capital.

Mr. Giffen refers to this as follows: "There is a close connection between the short loan and the speculation in securities. The funds of the short loan market are employed partly in holding securities, and where these funds are diminished or increased from any cause, however temporary, there is an immediate effect on the price of some securities. But the great mass of securities will only be affected by more permanent changes in the rates obtainable for money in other markets."

In recent years the connection between the Stock Exchange and the banks has been of a more intimate

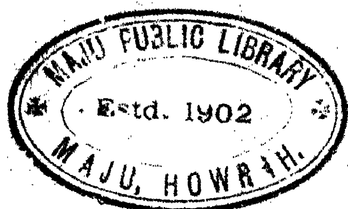
character. It has been stated by the *Economist* that an additional £9,000,000 of capital was lent by the banks on the Stock Exchange for the year 1889.

Large amounts of stock are deposited with the banks by stockbrokers against money lent for the fortnightly account, a certain margin being provided to cover contingencies. When the settlement arrives, a fresh loan is made and the stock is carried over for another fortnightly period. It is easy to understand how the rates for money must affect the price of securities which have not been bought by the public, and therefore do not represent actual purchases or sales.

Credit is also an important force in connection with the Stock Exchange. If at any time a rumour gets abroad that the banks intend to refuse loans on certain securities, the price of such securities falls considerably. The withdrawal of loans by the banks from the Stock Exchange would have a most disastrous effect. It was stated quite recently that certain banks intended curtailing their loans on the Stock Exchange, and even that rumour almost created a panic.

Any increase in the value of money would tend to increase savings, and as a large portion of such savings would be invested on the Stock Exchange, prices would therefore rise. On the other hand, a low rate of interest would act as a check on savings, and this effect is reflected in the price of securities.

The value of money in the market does therefore exercise a great influence upon all interest-bearing securities.



CHAPTER XVIII.

THE MONEY MARKET IN 1890.

In order to afford a practical illustration of some of the forces which from time to time cause fluctuations in the rate of interest, we intend to give a short account of the money market for the year 1890, because it was an anxious period for the banks of this country. In doing this we shall be able to judge somewhat whether the Bank directors exercised their powers rightly, in making alterations of the rate. We might notice that each year has some leading features which distinguish it from the preceding one.

Thus the failure of the City of Glasgow Bank in 1878 had an important effect upon the money market. Then again a gigantic speculation in some great commodity has an effect upon the rate of interest, such as the copper speculation in 1889.

Again, the requirements of a foreign country in order to place its currency on a satisfactory basis, which may lead possibly to a drain of gold, have caused great changes in the value of money. In fact we might almost say that the requirements of the world for specie, are supplied from Lombard Street. The year 1890 opened with a bank rate of 6 per cent., and also with the outside market denuded of capital, because the Bank return showed that the market had borrowed seven to eight millions. Of course this showed that the Bank of England had control over the outside market, and there-

fore little competition existed between the Bank and the said market. The year therefore began with a deficiency of surplus capital, in consequence of the heavy calls upon the resources of the market in previous years, which have been described as mania periods. Thus in 1888 £160,000,000 of capital was invested in South American securities, followed in 1889 by £190,000,000 of capital subscribed for breweries, mines and trust company investments. These facts explain to us the position of the market throughout the year. The consumption of capital has been larger than the supply.

Mr. Giffen has estimated the annual savings of this country to be £150,000,000, but of this amount a large portion would be invested in stock, premises, machinery, land, etc., and he therefore estimates that a balance of £80,000,000 can be regarded as free savings which require to be invested through the medium of the Stock Exchange. If, as he says, an additional £20,000,000 were added to any one year it would make a great difference in the prices of securities, which would be inflated, and paper profits would be large.

By means of these instructive figures we are able to ascertain whether the capital required for new undertakings is in excess of the annual accumulations. In order to show this we will take the capital called up for ten months to October, 1889, in comparison with the same period of 1890:—

October,	1889,	called	up	£128,670,798
,,	1890	,,	,,	104,729,709

From these amounts we should have to deduct the amount of capital returned to this country by means of redemption drawings. After making allowance for this return of capital, the figures given are very large in comparison with previous years.

For example, new issues of Colonial Government Municipal Loans, etc., were as follows, *viz.* :—

1876	£25,600,000
1883	48,700,000
1884	48,900,000
1885	51,700,000

We must therefore conclude that during the previous three years the amount of capital subscribed for new undertakings had been in excess of the annual savings. The above facts clearly show why a 6 per cent. rate was prevailing in January.

The first relief which the market obtained was through the payment of dividends on Government Stocks on 5th January, amounting to £5,250,000. These quarterly payments on Government Stocks are always taken into account by the money market and naturally tend to ease rates.

In the first quarter of the year there is another force at work which must not be forgotten, and that is the collection of taxes for the revenue. As the financial year ends on the 5th April, the collectors of taxes make strenuous efforts to obtain payment of all outstanding amounts. The revenue receipts for the quarter are about £31,500,000, and if the Chancellor of the Exchequer lends any of this amount, it would tend to lower rates.

The power of the Government in the money market must not be forgotten in considering fluctuations of the rate of interest. The Government borrows on Treasury bills, and whenever they are paid off or renewed, we have some changes in the rates for money.

Every week we find reference made to the two rates prevailing, *viz.*, the bank rate and the market rate, and sometimes when there is a great difference between the two, the Bank of England endeavours to make its rate

more effective by borrowing in the outer market. This is effected by borrowing on stock, which denudes the market of surplus capital. If we study the weekly balance sheets of the Bank of England, this result is shown in a decrease of Government securities.

For example :—

October 29 . .	Government securities . .	£16,133,500
November 5 . .	Do. . .	15,498,500
	Decrease	£635,000

This amount, *viz.*, £635,000, would represent the amount borrowed in the open market by the Bank.

Another important element to be remembered is the rates for money prevailing at places abroad where capital is concentrated. These rates tell us whether capital is likely to be drawn away from this country. They are quoted weekly in the *Economist* in the following form, *viz.* :—

Paris	+ $1\frac{2}{16}$	per cent.
Berlin	− $\frac{1}{4}$	,,
Amsterdam	+ 2	,,
New York	− $25\frac{1}{2}$	,,

+ (above) − (below) London rates.

The foreign exchanges also indicate whether capital is drifting towards this country or not. For example, we find a quotation as follows, *viz.* :—

France	+ $1\frac{3}{8}$ for us
Germany	− $2\frac{1}{4}$ against us
Holland	− $3\frac{1}{8}$ against us
New York	− 4 against us

As a rule, the foreign exchanges follow the changes of the bank rate, rather than precede such alterations.

The Bank of France is able to retain gold by charging a premium, and therefore high rates of discount prevailing here are unable to attract it, if that institution wishes to maintain its reserve of gold.

As we have already discussed the composition of the reserve at the Bank of England, it will only be necessary to study the changes which occurred.

The stock of bullion and the reserve in the banking department in January were both low in comparison with previous years.

Thus :—

	31st Dec., 1879.	5th Jan., 1887.	5th Jan., 1888.	2nd Jan., 1889.	1st Jan., 1890.
	£27,601,000	£19,307,000	£20,164,000	£19,366,000	£17,782,000.
Proportion of reserve to liabilities .		30⅞ per cent.	38 per cent.	29¼ per cent.	27⅛ per cent.

There were other indications showing the expenditure of capital. For example, the clearing house returns, which are always studied by the market because they illustrate the condition of business in the country.

Of these returns the fourths of the months give us some idea as to the amount of bills in circulation, whereas those of the fortnightly settlements and the Consol settling days on the Stock Exchange illustrate the amount of speculative and investment business transacted in the country.

If the returns were falling off, they would show that less capital was necessary to carry on the business of the country, and we should expect to see a gradual reduction in the rate of discount.

The returns for 1889 showed an increase of £654,878,000, which indicated that capital was in great demand.

The high bank rate at the beginning of the year had the effect of turning the foreign exchanges in our favour. For example :—

	4th Jan., 1890.	11th Jan., 1890.
French Exchange .	1⅝ for us	1 for us
German	2¼ against us	par
Dutch	3⅛ ,,	2¼ against us
New York . . .	4 ,,	par

In the early part of the year the market was affected by a financial transaction which has occurred on several previous occasions.

In order to effect the conversion of the Russian debt from 5 per cent. to 4 per cent. it was necessary that it should be done when rates were low. A forced ease was effected by means of a million of gold being brought here, and this additional capital would temporarily affect the market.

The note circulation in March generally shows a contraction of £2,000,000 to £3,000,000 in consequence of money being required for revenue purposes. Although a 6 per cent. rate prevailed in the market, yet it had not the effect of attracting gold to this country. The Bank of England paid a halfpenny per ounce more for bar gold in order to draw capital from abroad.

The rate was however reduced to 5 per cent. on 20th February in consequence of an increase in the bullion at the Bank, and also because the banking reserve showed a proportion of 50 per cent. to liabilities.

When the bank rate is high, the traders of this country suffer somewhat, because most of the banks are guided by the bank rate in fixing their charges. It is therefore important to the trading community that a high bank rate should not exist when the reserve at the bank is abnormally high.

On 5th March the rate was reduced to 4½ per cent., the market rate being 3⅞ per cent. There was nothing of importance in favour of cheap money, because there were several calls due on new undertakings and the business of the country showed some improvement; however the rate was reduced to 4 per cent. on 12th March in consequence of an increase to 51 per cent. in the Bank's reserve.

As we have already remarked, there is a close connection

between the banks and the Stock Exchange, and all applications for new capital affect the rate of interest.

The following table shows the increase from 1885 to 1890:—

	£	One Quarter.
New capital applications	30,240,000	1890
,, ,, ,,	56,800,000	1889
,, ,, ,,	34,600,000	1888
,, ,, ,,	21,500,000	1887
,, ,, ,,	26,800,000	1886
,, ,, ,,	13,759,000	1885

The quarterly dividends due 5th April would affect the market in the same way as in January, and consequently the rate was reduced on 10th April to 3½ per cent., the reserve at the Bank being in the proportion of 43⅞ per cent. There was a further reduction, 17th April, to 3 per cent., the reserve being 45¼ per cent. This ease however was not prolonged, because we find that in the following week a withdrawal of gold on balance of £357,000 had taken place and the reserve had fallen to 44½ per cent. Of this gold £200,000 was shipped to Buenos Ayres, where financial difficulties existed. The market also expected that the Russian Government would send its surplus capital from London to Paris, where most of its securities were held. This withdrawal of bullion had the effect of hardening market rates, especially when it was known that gold would also be required for Scotland in the following month, *viz.*, May, in order to meet payments due on the Scotch quarter day.

The Bank of England returns for 1st May showed that the market was short of capital, because applications had been made at the Bank for loans. This was shown by an increase in the other securities of £1,358,000. Again, the Government had issued £1,500,000 of Treasury bills, which would cause the withdrawal of surplus capital

from the market. On the other hand, it was known that £2,000,000 of Treasury bills falling due at a later period would not be renewed and therefore tend to ease rates.

The market at this time was somewhat affected by speculations in silver. This was in consequence of the United States authorising the coinage of additional silver. The sudden rise in the price of that metal naturally followed, and the price of all silver securities rapidly rose. It was stated that several large financial companies had speculated in such securities.

The effect of the silver legislation in the United States would cause gold to leave that country and increase the stock here. This is in accordance with Gresham's law, which states that if two metals are used as currency in a country, the one of less value will remain, whilst the other is exported.

It was also observed that the high bank rate in January and February had affected the value of the securities quoted on the Stock Exchange, where 7 per cent. was charged for loans.

On the other hand, the United States securities had risen considerably in consequence of the silver legislation. However, a few months later a reaction occurred, which showed that any attempt to give an artificial value to silver must fail.

With regard to the Stock Exchange, the cause for anxiety was the state of affairs in the Argentine Republic, where £150,000,000 of English capital had been invested. This would naturally affect banks and their rates of interest, especially as it was estimated that £9,000,000 of additional capital had been lent on the Stock Exchange.

There was nothing, however, to show that a great stringency would take place in the autumn, although the reserve of gold in the bank was £1,000,000 less than in

the previous year. In fact it was predicted that no great drain of gold would take place in the autumn, but if we remember the vast amount of new undertakings which absorbed the floating capital of the market, we cannot wonder at subsequent events.

The return for 12th June showed a reduction in the reserve to $41\frac{7}{8}$ per cent. The bullion in the issue department was also low, *viz.*:—

Last year	£22,884,000
June 12, 1890	21,760,000

The Indian Council at this time called in money lent on the market, and the demands for loans from the Stock Exchange were large. We therefore find that the market rate was only $\frac{1}{4}$ per cent. below bank rate.

The next weekly statement showed a reduction in the reserve to 39 per cent., the bullion being £300,000 less, and consequently the rate was raised on 25th June to 4 per cent.

At this time a large loan for the Argentine Government was expected, but it was found impossible to float a loan in the market, and this no doubt hastened the crisis in November.

The increased value for capital here caused a competition for bills by foreign lenders, and had the effect of reducing market rates.

We have already remarked that the investment of foreign money in bills on London is a favourite investment by bankers abroad.

In the following week, *viz.*, 10th July, the market rate was equal to the bank rate. This was due partly to the suspension of specie payments by the National Bank of Uruguay, and it was thought that specie would be shipped to the River Plate.

The rate of discount was raised to 5 per cent. on the

31st of July in consequence of a low reserve in the banking department, but principally due to a crisis in Argentina.

In addition to these facts, we must remember that a large number of new undertakings had been floated by syndicates, and the public not purchasing these new securities a large lock up of capital had followed.

The high bank rate attracted gold to this country in consequence of foreign houses competing for bills, and on the 21st August the rate was reduced to 4 per cent. Scarcely a month had elapsed before the rate was raised to 5 per cent., and although the gold reserve was low, yet no doubt the bank directors were guided in their decision by other events which were not realised until November.

The Stock Exchange settlements showed a large increase which was due largely to securities being sold to meet losses. For example:—

	1890. £	1889. £	1888. £
July 1 settlement	69,059,000	50,762,000	44,825,000
,, 2 ,,	60,970,000	47,525,000	53,009,000
Aug. 1 ,,	53,116,000	53,654,000	46,660,000
,, 2 ,,	59,403,000	48,673,000	45,068,000

The market rate being the same as the bank rate showed the scarcity of capital, and the Stock Exchange settlement for the first fortnight in October was concluded with great anxiety.

This settlement foreshadowed the collapse in November, because a great fall in South American securities had taken place. The bank directors realised the position of affairs, and on 7th November raised the rate to 6 per cent.

Money became very scarce, and in addition the market was full of rumours respecting the financial position of houses of world-wide repute. When it became known that the great house of Baring was in difficulties, it

seemed as if a panic would occur. Fortunately for the credit of this country, the governor of the Bank of England grasped the situation and endeavoured to maintain England's financial position. The leading banks agreed to form a guarantee fund, in order that the acceptances of Messrs. Baring, amounting to £15,000,000, should be paid as they fell due. The Bank of England also strengthened its position by borrowing £3,000,000 of gold from the Bank of France and £1,500,000 from the Russian Government. This had the effect of restoring public confidence, and what might have been a great crisis in our commercial history passed away, although the effect of the crisis was felt for several years.

It is satisfactory to observe that all the acceptances were paid, and the guarantors in 1895 were relieved of their liability. A company was formed to take over all the outstanding assets of Messrs. Baring.

The Bank also lent freely to those who required accommodation, although 7 per cent. and 8 per cent. was charged for such loans. This was shown by the other securities, which increased £6,079,000. Such high rates could not but fail to attract capital to this country, and when this was effected the rate was reduced in December to 5 per cent.

The year will always be a remarkable one in the history of finance, because of the new departure by the Bank of England. It showed that the other banking institutions are now so powerful that it is advantageous to have united action in order to avert a crisis. The commerce of this country is so dependent upon credit that it is desirable to have some protection for *bonâ fide* undertakings when an unsound system of finance creates a panic in the country.

We have endeavoured to show some of the causes which influence the bank rate, and how all the forces at work in

the money market are concentrated upon the reserve at the Bank of England. We have also observed that changes in the rate of discount are due to the movements of comparatively small amounts of capital, this being especially the case in the short loan market, where fluctuations occur daily in consequence of the requirements for capital being of a variable nature.

The cause of such changes is of great importance to the banks of this country, which not only lend their surplus capital in the short loan market, but also regulate their charges for loans somewhat in accordance with the bank rate.

It would be advantageous if the question of reserves, as affecting the rate of discount, was fully discussed by the representatives of the banks, in order to ascertain what amount of capital should be held to meet any contingency. If this question was thoroughly understood, we might have a less number of changes in the rate of discount, due to the absence or presence of small amounts of gold at the Bank of England. It might also prevent great discrepancies between the market rate and the bank rate, and thus tend to make the latter more effective.

Again, if bullion was required, the united action of all the banks would materially assist towards obtaining the metal from abroad.

CHAPTER XIX.

THE PRESENT SYSTEM OF BANKING.

WHEN we consider the old system of banking with that of the present day we find that a great change has taken place. In early times the issue of bank notes was considered the essential part of a banker's business. Nearly the whole of his profit was derived from this source. There is, however, a close connection between the issue of bank notes and the growth of deposits in the banks of this country. Any one who had notes in his possession would in course of time come to the conclusion that it is desirable to leave them with the banker for safety, and consequently would become a depositor. The issue of notes in this country has always preceded deposit banking. We have already remarked that one of the distinctive features of modern banking is that trade is now transacted by means of borrowed capital obtained from the bankers.

It was desirable that there should be a common form for the withdrawal of money deposited in a bank. The one adopted by the banks is known by the name of a "cheque," and this, in conjunction with bills of exchange, formed the medium for transacting the modern system of credit. The circulation of cheques has largely increased in consequence of the rapid development of trade, and also has somewhat superseded the use of bank notes.

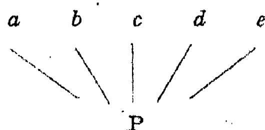
In 1844 the returns of the Clearing House were equal to 40 times the note circulation, but in 1872 these returns were equal to 135 times the note circulation.

1844	Proportion of notes to clearing circulation				= 40
1868	,,	,,	,,	,,	= 87
1869	,,	,,	,,	,,	= 90
1870	,,	,,	,,	,,	= 97
1871	,,	,,	,,	,,	=113
1872*	,,	,,	,,	,,	=135

It is important to recognise the great economy of capital which has been effected by the development of banking. The use of cheques has to some extent diminished the metallic circulation, and the system of transfers between bankers and the establishment of the Clearing House have also economised the use of gold and notes.

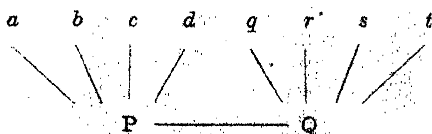
Mr. Jevons * gives the following account of the Clearing House system: "To obtain a clear view of the way in which bankers help us to avoid the use of money, we must follow up the rise of the system from the simplest case to the complete development of the complex organisation now existing in the United Kingdom".

The system of one bank would be as follows :—



Let *P* represent the banker and *a*, *b*, *c*, *d*, *e* his customers. Payments are made by one customer to the other by simply debiting and crediting. If *a* owes *b* money *a's* account is debited and *b's* credited.

The system of two banks would be as follows :—

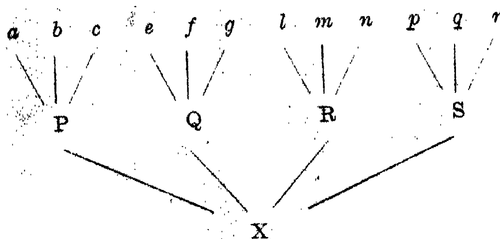


* *Money and the Mechanism of Exchange.*

Let P and Q be two bankers in a town, a, b, c, d being customers of P, and q, r, s, t customers of Q. Now the mutual transactions of a, b, c, d will as before be balanced off in the books of P, and similarly with the customers of Q. But if a has to make a payment to q the operation becomes more complex. He draws a cheque upon P and hands it to q. Not wanting coin he carries the cheque to his own banker Q and pays it into his account. There will be other persons in the town having to make payments in the same manner, and the probability is very great that some of these will result in giving P cheques on Q and some in giving Q cheques on P. The two bankers will then balance their mutual indebtedness by a single transaction.

In a town with several banks the system is still more complex. The several banks need only to agree to appoint as it were a *bankers' bank* to hold a portion of the cash of each bank, and then the mutual indebtedness may be balanced off just as when a bank acts for individuals.

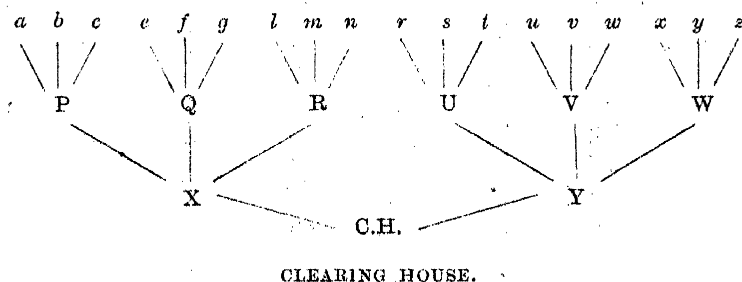
This is the system of the Clearing House. The bankers' bank is the Bank of England, but the accountant's part of the work is carried out at the Clearing House.



Let P, Q, R, and S = four banks, each with its own

body of customers, and X = the Clearing House. P need not now send a clerk to present bundles of cheques upon Q, R, and S, but can pay them into the Clearing House, and by a system of balances their mutual indebtedness can be discharged. The balance is paid by a transfer in the books of the Bank of England.

Only one further step is required to complete the system of connections between each bank in the kingdom and all other banks. Each country bank has a running account with some city bank, and all the city banks daily settle transactions with each other through the Clearing House. It follows that a payment from any part of the country to any other part can be accomplished through London.



CLEARING HOUSE.

Let P, Q, R be country banks, having the London agent X, and U, V, W, other country banks, having the London agent Y. If a, a customer of P, wishes to pay r, a customer of U, he transmits by post a cheque upon his banker P. The receiver r pays it into his account with U, who, having no direct communication with P, forwards it to Y, who presents it through the Clearing House on X, who debits it to P and forwards it by the next post.

This system of country clearing was instituted in 1859, chiefly through the exertions of Sir John Lubbock.

In consequence of the new system about £5,000,000 of gold currency was not required for the purpose of circulation.

The Clearing House was first started about the year 1775, when a few of the city bankers hired a room where the clerks from each bank could meet to exchange their bills and notes, and the differences were then settled by money.

The joint-stock banks were not admitted until the year 1854, but all the metropolitan banks in London are not, however, represented at the Clearing House. The Bank of England does not pay its own cheques through the medium of the Clearing House, although it presents all cheques on clearing bankers. The west-end bankers and the various branch banks of the metropolis use the Clearing House indirectly by giving cheques drawn on a clearing banker.

There are three daily clearings, *viz.:* 1st, at 10·30 A.M. for bills; 2nd, at 12 noon for country cheques; and 3rd, at 2·30 P.M. for bills and cheques.

In the year 1839 the average daily transactions amounted to £3,000,000. The balances were then settled by the use of £200,000 in bank notes and coin, to the amount of £20. The use of notes and gold is now entirely abolished, and the daily balances are settled by transfers on the Bank of England—each banker keeping an account with that institution.

The following table shows the increase in the transactions at the Clearing House:—

	£
1868	=3,425,000,000
1870	=3,914,000,000
1875	=5,685,000,000
1880	=5,794,000,000
1885	=5,511,000,000
1890	=7,801,000,000
1894	=6,337,000,000

The returns for the 4th of the month show to some extent the bill transactions of the country:—

	£
1868 =	155,068,000
1870 =	176,187,000
1875 =	245,810,000
1880 =	236,809,000
1885 =	221,873,000
1890 =	289,107,000
1894 =	261,501,000

In Edinburgh and Dublin the representatives of each bank meet for the purpose of exchanging their notes, upon the same principle as the London Clearing House.

There are provincial clearing houses established at Birmingham, Leicester, Liverpool, Manchester and Newcastle-on-Tyne. The amount cleared at such places in 1895 was £374,856,000.

CHAPTER XX.

BILLS OF EXCHANGE.

THE history of the growth of English industry and commerce reveals to us a series of causes which have materially contributed in constructing a highly complex machine, which we designate as the product of industry. Capital (or, in other words, wealth) did not exist in very early times, because then the land was cultivated simply for the purpose of supplying mutual wants. In those days the community satisfied their requirements by means of a system of barter or exchange. However, it was soon discovered that a system of barter had many inconveniences. The articles to be exchanged did not always satisfy mutual wants, and there also existed the difficulty of defining the ratios or value of each commodity. A medium of exchange was therefore necessary which would be accepted as payment for goods bought or sold, besides acting as a standard of value.

The precious metals, in consequence of their scarcity and other qualities, became at an early period the medium of exchange and a standard of value. Now as people became possessed of wealth they accumulated the precious metals, because by their means various needs could be satisfied.

A system of hoarding became common. Gold and silver coins were deposited in strong chests, and represented the capital of many individuals in this country.

There was scarcely any outlet for the surplus capital of

the country even in the reign of Charles I., and the Church at an earlier period prevented capital from being utilised by declaring it sinful to lend money at usury.

The business of money lending was in the hands of the Jews, who, however, derived their authority for so doing from the ruling sovereign. Whenever the early kings of this country required money they resorted to the Jews for assistance.

It was not until the people accumulated wealth that a system of credit was established. We have therefore first a possession of capital which found its way in course of time into the storehouse of capital or banks, and then followed a development of capital effected by means of credit documents or bills of exchange. Perhaps, therefore, the most important factors connected with the study of capital are banks and bills of exchange. We have already seen how the former have contributed towards promoting the material prosperity of this country.

It seems to us somewhat strange that the early bankers, or, as they were then called, goldsmiths, had no dealings in bills of exchange, those instruments of credit being utilised by the Jews for the purposes of money lending. However, in course of time banking and bills of exchange became indissolubly united.

We can scarcely comprehend how the early bankers transacted business without the medium of bills of exchange, when we consider what is effected in the present day by means of these credit documents. It is worthy of notice that as the method of banking underwent a change, so also the use of bills of exchange became somewhat different in character.

For example, the earlier bankers were goldsmiths, who received money for safe custody, and gave in exchange notes which remained in circulation, and thus through the

medium of such notes the goldsmiths became possessed of capital which they lent at interest.

It is also worthy of notice that this system of note issue laid the foundation of the modern system of cash deposits. We can easily see how this occurred. The note holder in course of time would discover that it was advantageous to deposit the notes which he did not immediately require with the banker, not only for the sake of safety, but also for the purpose of receiving interest on his surplus capital.

The goldsmiths became, in the modern sense of the word, bankers, when they could issue notes which would remain in circulation.

In like manner, bills have undergone a change in character. The earlier forms were drawn to facilitate the transmission of money from one country to another, but in course of time they were used for other purposes, such as methods of payment for goods bought or sold, for great financial operations, and also for settling international indebtedness. We shall show that the modern trade of this country has been greatly developed by means of credit documents, and, as a natural sequence to this, we have a corresponding increase in the business of banking.

CHAPTER XXI.

EARLY HISTORY OF BILLS.

THE early history of bills is of great interest, because we learn that from a remote period a need was felt for something which should take the place of metallic money for the purposes of transmission. Gold and silver coins could only be sent from one place to another at great risk. The Romans recognised the use of bills, and made it legal to sell a debt due from one person to another. If a debt could be sold it was desirable to have some means of transferring it. A written document was therefore necessary in order to transfer debts due, and these documents known as bills of exchange were in reality debts owing from one person to another.

Cicero says: "*Sed quæro quod opus illi erit Athenis permutarine possit an ipsi ferendum est*". We have therefore evidence showing that the Romans understood the utility of bills and transferred debts by means of them. Bills were used by the Italian and Jewish merchants, and in the fourteenth century were largely in circulation. Thus in order to trace the early history of bills and of banking institutions, we must go to the shores of the Mediterranean.

The utility of banking and bills of exchange was recognised by the Italians long before the system of credit was recognised in this country. The merchants of Genoa, Florence, Venice and other Italian towns sent their ships to the East with goods and received in exchange

gold and silver coins. The merchants then deposited their surplus wealth in the "mounts," or public treasuries, and received in exchange documents stating the amount deposited.

With the increased trade of the country it was necessary to have credit documents in order to facilitate the payment for goods between the various towns which traded with one another. When, therefore, bills of exchange became to be used for this purpose, they were the means of extending the operations of banking.

In these Italian towns banking was of two descriptions, *viz.*, one for money changing, acceptance of deposits, and transfer of accounts ; the other was of a private character, *viz.*, the lending of money and the discounting of bills. In the former case the municipalities undertook the business of banking, and in the latter the Jews or Lombards were the money lenders.

The use of bills was, therefore, principally in the hands of the Jews, who also found these documents very advantageous when they wished to transfer their capital from one place to another. This was needful, because they were continually expelled from various countries. Another circumstance must not be forgotten which materially increased the circulation of bills, and that was in consequence of the great power of the Roman Church. Each country had to contribute tithes to the pope, and these remittances were made either in specie or bills of exchange.

The growth and development of credit documents was also due to a race called the Lombards, who gave the name to a street in London which we might say has become the centre of the financial world. These Lombards were Italian merchants, and were descended from the Longobards, who settled in Italy after the fall of the

Roman empire. They were merchants representing the four republics of Genoa, Lucca, Florence and Venice.

Edward III., in travelling through France, made use of one of the Lombard banks when in want of money, and received from the Bank of the Bardi 5000 mks., for which he gave an acknowledgment for 7000 mks.

In course of time these Italian merchants established themselves in London, but at first they did not discount bills, that business being in the hands of the Jews. However, when the Jews were expelled from London, the Lombards became money lenders. It must also be remembered that public opinion had somewhat changed with reference to lending money at usury, because it was no longer considered immoral to receive interest for loans of capital.

The Record Office gives us an interesting example of an early bill. It was a bill drawn 26th September, 1442, by Francesco Venier & Bros., sons of the late Santo, at usance on Obertino de Bardi & Co. in London, and payable to themselves; value received in Venice from Cosmos de Medici & Co., and to be placed to the account of Marino Velliero at the exchange of 44½ per cent. per ducat, and the protest is signed by the notary public, Nicolar Acon, by imperial authority, on the 31st December, 1442, Anglican style, *secundum cursum et computationem Ecclesiæ Anglicanæ.*

The above bill illustrates that many of these credit documents were passing between England and Italy at that period.

Bills are said to have been first used in England in the year 1307, and were recognised as a *legal* method of sending money from England to foreign countries (Act 4, Richard II.).

The early history of bills therefore shows that they were

principally used for the purpose of the transmission of money, but they were also utilised for the payment of wages and for the payment of debts due from one person to another. It must be remembered that there were few banks in existence during the seventeenth and eighteenth centuries, and therefore banking facilities were comparatively unknown. The private bankers issued notes, but the amount in circulation was small in proportion to the population. A want was experienced of some circulating medium, and we therefore find bills used as bank notes, as well as for the payment of wages.

A practice was established by which the wages of servants were paid by means of promissory notes. It seems, however, that the system led to abuses, because bills were issued for such small amounts as 6d. and 1s., and when they were unpaid the loss fell upon poor people who could ill afford to lose. This system was happily confined to Yorkshire, but an Act passed in 1775 prohibited the circulation of promissory notes of less than 20s.

CHAPTER XXII.

MODERN HISTORY OF BILLS.

ALL the great changes connected with banking and credit documents have occurred during the present century. It has witnessed the formation of joint-stock banks and other kindred financial institutions, in addition to a great development of the modern system of trade based upon credit.

At the beginning of the century we find bills of exchange largely used in order to carry on the business of the country. These credit documents were more of the character of bank notes.

Mr. H. Thornton gives a very clear account of the great uses of bills of exchange. He says: "These documents obviate the necessity of sending gold from one place to another. Let us suppose there are in London 10 manufacturers, who sell their articles to 10 shopkeepers in York, by whom the said articles are retailed; and that in York there are 10 manufacturers, who sell their goods to 10 shopkeepers in London. This trade can be managed by transfers.

"Letters ordering the transfer of the debt are termed bills of exchange. They are bills by which the debt of one person is exchanged for the debt of another, and the debt, perhaps, which is due in one place for the debt due in another. These bills can be converted into money or they are discountable. Bills are also accepted as payment, although having some time to run. To possess some

article which so long as it is detained shall produce a regular interest, which shall be subject to no fluctuation in price, which by the custom of commerce shall pass in certain cases as a payment and shall likewise be convertible into ready money by the sacrifice of a small discount, is the true policy of the merchant. Liverpool and Manchester effect their business by bills at one or two months drawn on London. The bills annually drawn by the banks of these towns amount to many millions. The banks obtain a small commission on the transaction. Bills are drawn on London from every quarter of the kingdom, and remittances are sent to meet them. While London draws no bills, or next to none, upon the country, London has become the trading metropolis of Europe, and indeed of the whole world."

We have also an interesting account showing the development of private banking in the country, and the manner by which bills of exchange came into the hands of these bankers. A hundred years ago travelling in this country was attended with many difficulties; consequently, the transmission of money was somewhat risky. The people, therefore, found it advantageous to leave their surplus capital with the shopkeeper on market days, rather than run the risk of carrying it home. The country shopkeepers occupied an important position in the towns. They drew bills on London and also sent remittances to the metropolis. They would occasionally give gold to their customers, taking in return bills on the metropolis, which were then remitted with other bills to London correspondents. People who required cash for their credit documents obtained it from the shopkeeper, who charged something for the transaction. The shopkeeper then printed "Bank" over his door, and engraved these words on the cheques upon which he drew his bills. Money was

also taken on deposit at interest and utilised in discounting bills.

In the early part of this century, bills were largely used in Yorkshire for the payment of debts among the small manufacturers and among the dealers in wool, cattle and corn; and were in amounts of £10 to £30, and were proverbial for their dirty appearance and the number of endorsements. The most important point in connection with them was that they were very rarely unpaid.

Mr. Leatham in 1841 stated that "bills perform every function that can be assigned to the notes of the Bank of England, with a quality to make remittances by post which the notes cannot possess; and the only specific difference between them is that a limited time is attached to one and not to the other. But when at maturity bills are converted into gold with as much legal certainty as bank notes; when the origin of bills is *bonâ fide* and legitimate, I place them with the security of the drawer, acceptor, and perhaps twenty indorsements on the back, in the first class of our currency, before notes, and next to gold. I know of no purpose of money except wages to which bills are not applicable, in the provinces throughout this kingdom, though not seen in London in making payments. It is in the recollection of many persons that all the woollen business of the West Riding was conducted by bills of exchange at two months' date, as low as £5, drawn without stamps, with gold for wages, without the intervention of bank notes, previous to the last war."

We have, therefore, evidence showing that the country bankers in the early part of the present century transacted their business by means of bills of exchange, and also considered that the said instruments performed the functions of a currency.

Various Committees of the House of Commons, in dis-

cussing the position of the Bank of England and the state of the currency, referred to bills as an important factor with regard to these questions. Thus in 1810 and in 1819 some interesting facts relating to bills were published, and again in 1832 Mr. Burgess stated that a contraction in the quantity of bank notes in circulation produced directly a much greater relative contraction in the volume of the bill currency. Again, in 1840 Lord Overstone stated: "I consider the money of the country to be the foundation, and bills of exchange to be the superstructure raised upon it. I conceive that bills of exchange are an important form of banking operations. Bills of exchange, being an important form of credit, will feel the effect of that contraction in a very powerful degree."

The evidence given tends to show that bills were regarded as playing an important part as a circulating medium. Not many years had elapsed in the present century when it witnessed a great development in the use of credit documents. This became necessary in consequence of a great growth in English commerce, and assumed the form of a development of credit. Now credit has effected a complete revolution in trade. It has been the means of economising our metallic circulation and also assisting to transfer the capital of the country from hand to hand. Great facilities were required in order to conduct the modern trade based upon credit, and this was effected by the formation of joint-stock banks. The surplus capital of the country found its way into these new institutions, and was transferred from districts where it was not required to other places where it could be utilised at a profit. The formation of joint-stock banks therefore increased the bill circulation of the country.

According to a statement in 1881 by Mr. Pownall, the following were the proportions of cheques, bills, etc.:—

LONDON CLEARING BANKS.

Cheques through the Clearing House	71·313	per cent.
Cheques and bills not cleared	25·248	,,
Bank of England notes	2·349	,,
Coin	·956	,,
Country bank notes	·134	,,
	100·000	,,

At the Army and Navy Stores the proportions for 1880 and 1881 were as follows:—

	1880.	1881.
Cheques	63·67	67 per cent.
Notes	18·6	13·7 ,,
Coin	17·8	19·3 ,,

excluding postal orders and notes.

The foreign trade of the country has greatly developed during the present century, partly due to an increase of capital and also in consequence of the adoption of free trade principles by this country. Goods purchased abroad were paid for by means of bills drawn payable in London.

The new system of credit shows us that we have banks and paper documents, *viz.*, cheques and bills of exchange utilised for the purpose of transferring capital from one person to another.

So great has been the use of credit documents in recent years, that it was stated by Sir J. Lubbock that 97 articles out of 100 paid into the bank consisted of cheques and bills. The credit documents which concern us, *viz.*, bills of exchange, denote that property is bought and paid for either by the transfer of a debt or a promise to pay later, based upon goods bought or sold. The ability of the banker to lend in reality depends upon the state of trade, and consequently upon these credit documents. For example, bills represent a variety of transactions in every department of trade, and according to the productiveness of these trades the banker has either more or less to lend. By reference to these credit documents we

can ascertain whether certain industries are prosperous or depressed. For example, if a trade is thriving we should expect to find in the banker's bill case a large number of bills representing trade transactions in that particular industry; but if on the other hand there is a depression, a less number of bills would be in circulation.

It is sometimes difficult to ascertain what are the purposes of the vast number of bills which pass through the banker's hands. Do they always represent legitimate trade transactions, or are they the result of speculation? On several occasions in the history of banking, bills have been drawn against fictitious values.

Merchants accept bills drawn upon them for goods purchased, and incur liabilities on the supposition of being able to discount the bills received for goods sold at their bankers. If they are unable to do this, we can see how quickly trade becomes demoralised and the industrial machine thrown out of gear.

Our modern trade, conducted through the medium of banks and bills of exchange, reveals to us the fact that credit is very sensitive. For example, credit may be transferred into bad hands, that is, into those who do not understand how to use it to advantage. Again, it enables an unsound business to be carried on and fresh liabilities incurred, which without the medium of credit documents would cease to exist. We therefore lose in security what we gain in economy by the modern development of credit.

By the system of bills we might say that the whole body of traders become as it were associated with the banking community. The ability of the banker to lend is largely dependent upon bills being paid at maturity. Banks and the great instruments of credit, *viz.*, cheques and the bills of exchange, transfer the ownership of wealth from one person to another. We might say that bills of

exchange and banks are two machines for performing the same kind of work.

London has become not only the great financial centre of this country, but also of the whole world. The surplus capital in the country finds its way to London, and from thence is transferred to places where it can be utilised. All the great transactions of the inland trade are, we might say, concentrated in Lombard Street. The country banks send their surplus capital to the metropolis to be utilised in discounting trade bills. If these banks require additional capital to meet their requirements it is obtained by means of rediscounting these credit documents. London has also become the financial centre of the world. The number of bills drawn upon London surpasses any number drawn upon other countries.

The great metropolis therefore assumes the character of an international Clearing House. Our modern system of capital has laid the foundation of a new business, *viz.*, that of bill brokers.

In the early part of the century, London had become the centre for all banking transactions. In 1810 Mr. Richardson, who afterwards became a partner in the celebrated firm of Messrs. Overend, Gurney & Co., stated that the nature of an agency of a country bank was (1) to procure money for country bankers on bills when they have occasion to borrow on discount, and (2) to lend the money of the country banks on bills on discount. This system really meant the discount and rediscount of bills of exchange.

At first merchants acted as agents for the country bankers, but in course of time the bill transactions became so large that the business assumed a distinct form, and those who carried it on were known as bill brokers. At the same time there was a large increase in the

number of country banks which came into existence, partly in consequence of the London bankers, who were willing to act as agents at a less commission than originally paid to the merchants.

Every new bank which started in the country was the means of increasing the circulation of bills. The part played by the country banks was therefore an important one towards developing the bill transactions of the country. The country banker had, we might say, the majority of the bills in his neighbourhood passing under his notice. He was thus able to discriminate between good and bad paper, or legitimate trade transactions as distinguished from accommodation bills. The good paper was discounted by him, and possibly rediscounted in the London market. In this manner large transactions between London and the country were conducted, and business was stimulated by the action of the country bankers.

The late Mr. Newmarch in 1850 gave an interesting account of the London bill brokers who remitted bills to the country for the purpose of circulation:—

"B., a banker at Lincoln, has a surplus of £50,000. He is also in the habit of requiring bills of exchange of certain usances and of certain amounts to meet the applications of some of his customers who employ them in the course of their trade. B. might have bills in his own case, but would not reissue, because (1) it would indicate that he was poor, and (2) it would disgust his customers by revealing their transactions to rivals. The London bill broker therefore sends bills plus the amount of discount due by him on the transaction. These bills had been created in totally different parts of the country, some being foreign bills. This transaction between London and Lincoln accomplishes four things. The Lincoln

bank obtains (1) employment for money, (2) a good security; (3) the bill broker receives £50,000 by which he can discount a further amount; (4) a bill currency is introduced into Lincoln perfectly adapted to its wants.

"There are three principal modes in which payments of debts are accomplished: (1) The buyer may have no difficulty in placing his account upon the footing of a book debt where he is debited for what he purchases and credited when he pays; (2) buyer may pay his debts by remitting approved bills; and (3) buyer may undertake to accept bills drawn upon him by the seller. By the first and second modes the circulation of bills is promoted, and by the third mode the *creation* of bills takes place. The bills obtained from London may accomplish seven distinct transfers: (1) Discharges conditionally the claim of drawer or acceptor; (2) discharges claim of payee on drawer; (3) bill broker on payee, supposing the payee to discount the bill; (4) Lincoln banker upon bill broker; (5) farmer upon Lincoln banker; (6) dealer in goods or cattle on Lincoln customer; (7) when sent for payment by dealer's banker to London correspondent."

Mr. Newmarch concludes his remarks by stating that "this skilful redistribution of the bill currency of the country is one of the greatest achievements of our banking system".

This system has now become extinct in consequence of the altered conditions of trade. Bills are now sent to the country banks solely as investments, and not for currency purposes.

The amount of bills under discount by the banks of the country for the year 1849 was estimated as follows, *viz.*:—

	£
Scotland	15,000,000
Lancashire	12,000,000
England	60,000,000
	87,000,000
Foreign	13,000,000
	100,000,000
Not discounted	16,000,000
	116,000,000

We can quite understand that as the business increased in London in consequence of more bills being sent from the country, it was necessary that the merchants who transacted such business should devote their whole time to the study of these documents, and therefore the business of a bill broker became quite distinct. The vast number of bills which found their way into the London market were exceedingly difficult to understand, because they represented an infinite number of trade transactions. In order to estimate the relative credit of each individual whose name appeared on bills either as drawer, acceptor, or indorser, the modern bill broker devoted himself entirely to the study of these documents, which were classified as being either first or second rate. If of the former description it would be assumed for a certainty that at maturity they would be paid, but if of the latter class it might be otherwise.

This change in the system of business has affected the bankers, because, instead of relying upon the bills held by them, they depend to a great extent upon the broker. The modern bill broker also receives money on deposit, which is utilised in discounting bills. However, the position of the bill brokers is one of great delicacy, because they are dependent upon the bankers for a great portion of their funds. If at times the bankers have no surplus capital to lend, the bill brokers make application

to the Bank of England for loans in order to meet their requirements. Therefore the Bank of England is called upon at certain times to meet large demands upon its reserves.

The London bankers keep a large portion of their capital with the Bank of England, which has had the effect of making the Bank of England the final reserve for the country.

It is a part of the system of the Bank that any one respectably introduced can have a discount account at that institution. It seems an anomaly that the London bankers and the Bank of England should supply the bill brokers with funds in order to compete against them. We have seen that when the bill brokers are unable to obtain sufficient funds from the London bankers, they make applications to the Bank in order to meet their daily requirements.

Thus the Bank is called upon to meet a large number of applications for loans, which at times amount to a considerable sum. During the commercial crisis of 1857 the Bank lent to bill brokers more than nine millions, although their advances to the bankers amounted to only £8,000,000, and not unnaturally the Bank thought it unreasonable that so large an inroad upon its resources should be made by their rivals.

Another important point to be remembered is that some of the bill brokers carry on their business with a comparatively small capital in proportion to their great liabilities.

The bankers of the present day, by lending their surplus capital to the brokers, have been the cause of the latter class obtaining nearly the whole of the best mercantile bills; whilst the former now discount trade bills of smaller amounts, such as those drawn by the wholesale

houses upon the retail dealers in the country. The Bank of England has shared the fate of the other bankers in not being always able to obtain discount business. It may happen that the bank rate is say 2 per cent. when bills are being discounted in the market at ½ per cent. This explains to us the reason why at times the bank rate is ineffectual to attract gold from abroad. The London banks have lost in some degree what was considered one of the best investments for surplus funds in consequence of the present system of large loans to the brokers.

Another point for consideration is whether the money lent on demand to bill brokers can in reality be considered as a reserve. If a crisis in the money market should occur, and all the banks call in their loans, it would be impossible for the brokers to meet the demands without assistance from the Bank of England, and at such a period that institution might not be in a position to meet all outside applications.

The Bank of England is supposed to find capital at times when the outside market has exhausted its credit. That great institution being the final reserve for the country, makes it a very important factor in the money market, and its weekly accounts are closely studied.

The Bank's position in the discount market is at the present time somewhat different from what it was some years ago. The large increase in the number of joint-stock banks holding vast deposits which must be lent, has contributed towards the change. Thus in 1851 the Bank discounted £1 out of every £20 inland bills created, whilst in 1875 there were at least £30 of inland bills created for every pound of the same discounted by the Bank, and during the last twenty years the bill transactions are still relatively smaller. Competition is continually taking place between the Bank and the outside market, or in other words the bill brokers.

CHAPTER XXIII.

BILLS AND COMMERCIAL CRISES.

WE have seen that the formation of banks and a great development in the use of bills of exchange acted as a stimulus towards increasing the trade of the country. On the other hand they have been utilised during periods of speculative activity for the purpose of promoting new undertakings, and have thus contributed at various epochs in the history of British commerce towards producing a commercial crisis.

We know that the trade of this country is attended with considerable risk. Goods are purchased and paid for by means of bills drawn at various dates. During the interval between the time when the bill is drawn and the day of payment, a series of events may possibly happen. For example, a great fall might have occurred in the value of the commodities against which the bills were drawn, or there might be a change in the state of commercial confidence or credit. Traders incur great liabilities and carry on their business upon the understanding of being able to discount bills at *all* times, without reference to other influences which may possibly disturb the money market. If, therefore, one of the links in our modern system of credit becomes broken, the result is sometimes disastrous.

Again, the division of labour has had the effect of making the various industries of the country dependent upon one another. If one industry becomes depressed, other industries are soon affected by the same depression.

Trade bills represent risks both in time and space: in time when a merchant purchases goods to sell at a higher price at some future date, and in space when goods are purchased to be sold in a distant market. There are, however, less risks in the inland than in the foreign trade. Goods manufactured and sold in this country represent transactions for short periods, whereas in the foreign trade a longer period elapses between the purchase and the sale of goods. We know also that markets fluctuate considerably, even in a month.

In 1869 74 per cent. of inland bills were for amounts of less than £100, whilst the foreign bills showed only 47 per cent. less than £100, the bulk being from £400 to £4000.

Trade, therefore, being conducted principally through the medium of bills, it follows that the number in circulation would be a good index as to the condition of English industries. The transactions at the Clearing House on the 4th of each month, that being the principal day on which bills mature, would tell us somewhat whether trade is active or depressed.

The late Mr. B. Price stated* that it is sometimes difficult to ascertain the forces which lie underneath the vast number of bills passing through the bankers' hands. Do they represent legitimate trade transactions or those of a speculative nature?

It is, therefore, important that the banks should study closely the credit documents which come into their possession.

* *Currency and Banking.*

Mr. Hankey states that a banker should know the difference between a mortgage and an ordinary bill of exchange. An ordinary bill has such a provision or security. It is based on the transfer of capital in some shape or other in a manner which contemplates that at a fixed date such capital will have passed into the required hands, and that means will be provided to meet it. The other kinds of bills, which we may term mortgages, are based upon money being raised to meet them when they fall due.

CHAPTER XXIV.

CLASSIFICATION OF BILLS.

THE different classes of bills with which banking is so intimately associated are varied in character.

We have noticed that a great proportion of trade transactions are effected through the medium of credit documents. Goods are purchased and paid for by means of bills drawn at various dates, either by a transfer of a debt due from one person to another, or by a promise to pay at a later date. If a banker looks carefully through the bills passing through his hands, he soon discovers that they represent various transactions.

The first division would be inland and foreign, the former representing the home trade, and drawn in this country, the latter representing the foreign trade, and therefore drawn abroad, but as a rule payable here.

Mr. Newmarch in 1851 classified the inland bills into three divisions, *viz.:* (1) Bills up to £50 of an average amount of £23 8s., with an usance of 2-8 months; (2) bills up to £300 of an average amount of £142 7s., with an usance of 3-5 months; (3) bills above £300, with an usance of 4 months and an average amount of £1206 3s. The third class would be bills drawn between merchants, producers and manufacturers and wholesale dealers and large consumers of raw material, or, speaking generally, between merchants and dealers. The second class would be bills drawn between houses of less extent of business and wielding a less powerful

capital, and also between large wholesale houses, and in general terms between dealers and retailers. The first class would be bills which belong to the retail trade, and may be described with considerable propriety as drawn between retailers and consumers.

The number of bills drawn on London from foreign countries is very large, and they are the means of discharging international indebtedness. Again, London has become the financial centre of the world, and therefore debts are discharged by means of bills drawn on London.

The foreign bills are for large amounts and are principally in the hands of the bill brokers. These bills to a great extent represent the proceeds of foreign loans, and also payments for interest on money raised in this country. The enormous transactions in foreign bills are an additional element in banking business which may exercise a very great influence at any time.

When we consider the magnitude of these financial operations effected by means of credit documents which find their way into the banks, we are astounded at the wonderful system of finance by which all payments are punctually met.

There has been a large increase in the amount of bills in circulation during the present century. Various estimates have been given; the first was by Mr. Leatham, and afterwards by Mr. Newmarch and others:—

	£	
1832=	89,000,000	......
1839=	132,000,000	......
1843-6=	116,000,000	(Mr. Newmarch)
1856=	180,000,000	Do.
1870-1=	300,000,000 to 350,000,000	(Mr. Palgrave)
1881=	1,373,425,920	(Mr. R. W. Barnett)

There would be some difficulty in estimating the amount now in circulation, because the Government returns

include stamps for bills, postage and other purposes. It is to be regretted that some of the banks do not separate in their balance sheets the amount of bills held in proportion to other advances.

Mr. John Dun estimated some years ago the amount of bills held by the banks from the returns of those which separated bills from other advances, as follows:—

Scotch banks . .	60 per cent. of bills to			40 per cent. of advances.		
Irish banks . . .	69	,,	,,	40	,,	,,
Purely London . .	30	,,	,,	70	,,	,,
London and Provincial	50	,,	,,	50	,,	,,
Purely Provincial .	50	,,	,,	50	,,	,,

According to a recent statement in the *Economist*, there has been a great decrease in the amount of bills in comparison with advances.

BANKS OF UNITED KINGDOM.

	1895. £	1894. £
Discounts	42,632,000	37,003,000
Advances	116,745,000	109,422,000

The following estimate of bills discounted by the banks was given by Mr. Dun:—

	£
Bills discounted	274,300,000
Less bills rediscounted	30,000,000
	244,300,000
Bills held by foreign and Colonial banks, and undiscounted, in private hands . . .	80,000,000
	324,300,000
Bills held collaterally against advances and acceptances	20,000,000
Amount of bills in circulation =	344,300,000

In a recent address by a vice-president of the Institute of Bankers (Mr. Birch) it was stated that, from published reports, the bills discounted by the banks are now less than they were nine years ago. He says: "From the

published reports it would appear that certain banks (excluding the Bank of England), with 100 millions more of deposits, paid-up capital and reserves than they had nine years ago, have increased their discounts by only £8,000,000, and that the proportion of discounts to the total assets which in 1880 was 26 per cent. has now fallen to 21½ per cent. The amount of bills taken off the London market by discount daily was estimated by Mr. Palgrave to be £3,000,000.

The number of bills passing through the banks is so great that it has been found necessary in all the large banking institutions to have a separate department, where all matters appertaining to such credit documents are effected.

In a London bank, the bill transactions would represent a medium by which the trade of this country is carried on. Bills discounted are perhaps the most important of credit documents held as security for money lent. These documents would be closely examined in order to ascertain whether they have been properly executed, The banker would also make inquiries as to the standing and position of the various parties, and keep a record of the information so obtained.

Another class of bills are those left for collection and designated "short," because of their having only a few days to run.

Again, bills sent up for collection by the country banks would form another division, and are presented for acceptance if requisite.

Then we have bills drawn by the country bank on its London agent and which require acceptance. The London banker also receives foreign bills for sale in the market at the exchange of the day.

Another class would be those drawn abroad by

foreign correspondents on their London agents. These bills are known as acceptances in the market, and are of so much importance in modern banking that it will be necessary to show how they differ from ordinary trade bills. Some of the bills drawn abroad by foreign correspondents are utilised for the purpose of profiting by the variation in the exchanges upon England. Again a large number of bills payable in the country are also left with the bankers for collection.

The London banks are so intimately connected with the bill brokers that the former have always a large number of bills left by the latter as security against money lent at call.

The bill brokers now take bills payable in the country, if first class, and such bills have to be collected at maturity. All the various transactions connected with these documents require time and attention. The banks ascertain whether they are drawn upon proper stamps, and whether the acceptances and endorsements are in order; the due date of each bill is also marked upon it. It is very important that they should be presented for payment at maturity, and if not paid it is necessary either to note or protest for non-payment.

Another class would be those conditionally accepted, that is, to be paid on production of bills of lading and shipping documents. We have therefore bills representing transactions all over the world being negotiated daily in every banking institution. The comparatively small number unpaid shows us how important these documents are as security to banks for money lent, and also as a medium for the payment of debts.

CHAPTER XXV.

DEVELOPMENT OF BILLS.

IN conclusion we will briefly discuss some points of interest relative to bills which are of most importance in connection with the daily transactions of banks in these credit documents.

In the first place it is necessary to know something of the law relating to bills of exchange.

We have noticed previously that bills were a legal method by which money could be sent from London to foreign countries in the reign of Richard II. Subsequent to 1770 bills of small amounts circulated as bank notes. This was in consequence of an absence of banking facilities in the country. Bills of less than 20s. were in circulation and were utilised for the payment of wages. However, it was found that many of these small bills were unpaid and the loss fell upon the poorer classes. An Act was passed in 1775 prohibiting their use.

Mr. Chitty states that bills and promissory notes were not assessed with stamp duty in England before 1782, when the special exemption of 5 Will. and Mary, cap. 21, sec. 5, was repealed by the Act 22, George III., cap. 33, and scales of duty were imposed.

Subsequent Acts of Parliament increased the duties payable on the issue of bills. The most important Act relative to them is that of 1881, which codified the existing law relative to credit documents.

The basis of the law is founded upon a series of judicial

decisions which were determined by the customs of trade. Mr. Chalmers states that the great bulk of the law relating to negotiable instruments is contained in the reported cases, which are very numerous. The last edition of Byles on bills cites more than 3000 cases. Contrary to the general rule in the law of England, the benefit of a contract arising on a bill of exchange is assignable and consideration will be presumed unless the contrary appear.

We have seen that they were used in England in the reign of Richard II., but the first recorded decision regarding them occurred in the reign of James I.

The courts for a long time regarded bills with jealousy as an exception to the common law, and restricted their use to merchants, but at last their obvious utility overcame the scruples of the judges. A bill of exchange is defined by the Act of 1881 to be "an unconditional order in writing addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand, or at a determinable future time, a sum certain in money to or to the other of a specified person, or to bearer". Every indorsement on a bill really constitutes the indorser as a new drawer, and the indorsement admits the signature and capacity of every prior party, so that every indorsement on a bill is to a banker an additional security unless an indorsement is forged, which would have the effect of cancelling subsequent indorsements.

The custom of making bills payable at a bank is comparatively modern, and a holder could object to receive a bill so accepted.

Of course it is a great convenience for traders to make their bills payable at a bank, but unless there is a special agreement between the banker and his customer it is doubtful if the latter could make any claim against the

former in case of refusal to pay bills. A banker is compelled to pay cheques providing he has funds belonging to his customer, but a bill of exchange is outside the relation of a banker to his customer.

The banks ought to consider whether it is desirable for them to undertake great risks in the payment of bills for their customers, when they are held liable for forged indorsements. It is impossible to verify indorsements, and therefore the law relating to bills ought to be assimilated to that of cheques, so that the banker should be protected in case a bill is paid with a forged indorsement.

The French Code protects bankers if bills are paid with forged indorsements.

As a protection the banks might decline to pay cash over the counter for bills made payable at their offices.

It is not an uncommon procedure in London for bills to be presented for payment and bank notes obtained in exchange, in order to wire the fate of such documents.

Another mode of protection might be obtained if the banks insisted that bills should only be paid with cheques attached. Of course safeguards such as these are not beneficial to the trading community, and therefore if the law could be assimilated to that of cheques no change of custom would be requisite.

As bills also form the method of settling international indebtedness, it would be advantageous if the law with regard to those instruments was identical throughout the world.

In France a bill represents a trade transaction, and therefore it does not circulate.

The bill must state on its face that value is received in goods, value received in cash, or value in account. In this country the law raises a *prima facie* presumption that value has been received.

Several interesting discussions relating to bills took place at a meeting of the Institute of Bankers held 19th December, 1879. At that meeting it was resolved that it would be desirable to abolish days of grace, now that the means of communication are so rapid. This has recently been done in the United States. Another point discussed was, whether conditional acceptances might not be abolished. However, the meeting was in favour of their retention. These conditional acceptances, which are bills payable on the delivery of bills of lading and shipping documents, meet the requirements of the foreign trade of this country, and are therefore beneficial. The third discussion at that meeting was, whether it would be desirable to impose restrictions upon the issue and circulation of accommodation paper. The French and other Codes state that such credit documents are illegal.

It was decided, however, that it was not considered advantageous to interfere with the present law, because many bills which appear to be accommodation paper are in reality trade transactions.

It is important for a banker to know the position and liability of each party to a bill, so that, if necessary, he may be able to sue the right persons.

When an inland bill is unpaid, it is considered advisable to have the same noted, but foreign bills are both noted and protested. The latter course should always be adopted for foreign bills, but there is a tendency for inland bills not to be noted.

Our modern system of credit has been the means of utilising bills in order to obtain capital from the banks. This is effected by means of bills which, as a rule, are drawn by foreign correspondents, who deposit securities to cover the advances so obtained. They are known as acceptances, and are readily discounted by the bill brokers, and are known in the market as bank acceptances.

Mr. Dun has subdivided acceptances into the following classes:—

1. Drafts of seven, fourteen, or twenty-one days drawn by country bankers for the purposes of remittance.

2. Acceptances up to ninety days against credits established by banking correspondents in the country.

3. Acceptances on account of foreign and colonial banks having head offices in London.

4. Acceptances to mercantile firms and companies abroad.

Mr. Dun believes that the third class ought to be kept within bounds, and that the fourth class ought to be avoided altogether.

With regard to acceptances, there is always an element of danger, especially when a feeling of distrust exists in the mercantile world.

A bank which is perfectly solvent may have accepted a large number of bills against which it holds sufficient cover. When, however, a crisis occurs, the bills which have been accepted by that bank may be refused in the market, especially if there are a large number offered for discount. If this occurred the bank's credit may be materially injured, and, as a natural consequence, it may possibly lead to its failure.

One of the noticeable facts in connection with the City of Glasgow Bank's failure was that within a week after its acceptances had been refused in the market its suspension occurred.

Another risk with regard to acceptances is, that many changes may occur between the interval of acceptance and the day of payment.

The chairman of the London and Westminster Bank stated some time ago that "acceptances drawn by mercantile firms abroad is part of the business that ought to be carried on by a merchant or merchant banker".

It has been represented by those who are in favour of acceptances that if the business is kept within bounds it is perfectly safe, and those banking institutions which have transacted such business have made few losses. Of course, it is important that acceptances should be fully covered by means of the deposit of good securities in case of loss.

Acceptances may be utilised in order to effect Stock Exchange transactions; securities bought on the Stock Exchange being deposited as cover. This kind of business would certainly be discouraged by the banks.

The acceptances of six of the principal London banks show a considerable decrease:—

£
1880 = 9,470,000
1888 = 7,153,000

The acceptances of seventeen metropolitan banks show a great reduction during the last five or six years.

The amount to 31st December, 1894, was as follows:—

Purely Metropolitan	£7,334,000
Metropolitan and Country Branches . .	7,348,000

At the present time there seems to be a decrease in the amount of bills in circulation, which is partly due to the fact that modern trade is based principally upon cash transactions; many firms dealing with wholesale houses find it advantageous to pay cash for goods purchased rather than give a three months' bill. The trader then gets the benefit of the discount allowed by the wholesale firm for ready money.

The great increase in the business of co-operative stores, where all sales are for cash, has also been the means of lessening the number of bills. Formerly the trade transactions of the stores were in the hands of shopkeepers who sold goods on the credit system, and therefore were

not always able to pay cash for goods bought. Consequently the retail dealer was at times compelled to give bills to the wholesale manufacturer. It has been stated that during the busy season at a London co-operative store the daily receipts amounted to £10,000.

Again, the means of communication are now so rapid that it has materially assisted the present system of cash payments. Instead, therefore, of bills being used we find country cheques form the mode of payment. Cash can be obtained for these cheques through the medium of the Clearing House in the course of a few days.

The Clearing House statistics show a proportionate decrease in the amount of bills payable on the 4ths of the month, but a large increase in country cheques :—

CLEARING HOUSE RETURNS, 4TH OF THE MONTH.

	£
1875 =	245,800,000
1880 =	236,809,000
1885 =	221,870,000
1890 =	289,107,000
1894 =	261,547,000

PROPORTION OF 4THS TO TOTAL AMOUNT OF CLEARING.

1877 = 4·6 %
1892 = 4·0 %

There has been a large increase in the use of country cheques. According to the Clearing House returns the amounts were :—

	£
1884 =	443,000,000
1885 =	426,000,000
1889 =	522,000,000

In 1880 Messrs. Glyn, Mills, Currie & Co. cleared 19,950 cheques in one day, of which 2½ per cent. were under £1; but in 1887 they cleared 35,090, of which 4 per cent. were under £1.

Whilst, therefore, bills have decreased, there has been a large increase in country cheques.

Again, the system of telegraphic transfers has contributed towards decreasing the number of bills drawn.

Mr. Birch gives an interesting account showing how these transfers act as substitutes for bills. "Formerly the banks and great commercial houses in the East, in the United States and elsewhere took as they do now the ordinary trade bills, *i.e.*, drafts against documents of consignments and such like at six, four, three and two months at the ordinary usance, and any one requiring first class clean bills for remittance, either for the purchase of commodities or to cover credits or other purposes, would apply to these banking institutions who would give bills also at usance. Thus there were running two sets of bills representing one commercial transaction. Now these banking institutions continue to take these trade bills as formerly, but instead of drawing at usance they give telegraphic transfers, which enables a merchant in Hong Kong, or in New York, or in any other part of the world, to calculate exactly the cost of his operation, just as if he were sitting in London; no question of discount, of bill stamp or other expense, or whether the bill be a good one. He can balance his operation just as well at these distant places as if he were sitting in Lombard Street."

Bills are utilised in the present day in the manufacturing towns of the North of England for the purpose of settling trade transactions.

Thus the monthly settlements at Bradford, Huddersfield and Leeds are effected by means of drafts drawn upon London.

We have already noticed that the largest proportion of bills in circulation is in the hands of the bill brokers.

This is certainly one of the features of our modern system of finance. The large increase of business on the Stock Exchange has no doubt somewhat increased the number of bills in circulation. There is a less number of inland bills, but foreign bills are increasing. The foreign bills are utilised for the purpose of withdrawing capital obtained in this country for investment abroad.

Again, the payments of interest by foreign countries are made by means of bills of exchange. These payments are very large. For example:—

	Dividends.	Drawings of Bonds.
	£	£
1888	42,497,300	3,669,100
1887	43,101,700	3,608,600
Increase .	604,400	60,500

Although bills have increased for certain purposes, yet on the whole there has been a decrease, and this has somewhat affected the business of the notaries, who in former days were fully occupied in noting and protesting such documents.

It is certainly a cause for regret that the banks of this country do not discount so many bills as formerly. These credit documents are justly considered as one of the best investments for surplus funds. Mr. Hankey says that bills of exchange are the only kind of investments upon which absolute dependence can be placed for a return of capital at a fixed date.

Good commercial bills of short dates have this advantage over Government stock or exchequer bills, that a banker is sure to receive back the same amount of money which he advanced.

The high value set upon bills by bankers is shown by the large amount held by them as security against advances to bill brokers.

Again, they can be utilised for the purpose of re-

discount in cases of emergency or other reasons. Some bankers of the present day prefer keeping their reserves in bills rather than in Government stocks; for various reasons, therefore, a decline in the bill transactions of the banks is to be deplored.

In consequence of a decrease in these documents, the banks are increasing their loans on the Stock Exchange, but it is questionable whether this is a change for the better.

From the published reports of certain banks we find that advances which are largely made up of loans on the Stock Exchange have increased by 52 millions, and their proportion to the total assets has risen from 34 per cent. to 38½ per cent.

If all the banks separated their bills discounted from their advances, we should be able to form some idea as to the changes in the bill transactions of this country.

In the course of this inquiry we have endeavoured to show how bills were introduced into this country, their utility as a circulating medium for the purposes of trade, and how they came to be associated with banking.

In conclusion we may state that as instruments of credit they have contributed largely to promote the prosperity of the banking institutions of this country.

Bills have also assisted materially to promote the growth of English commerce, and have been the means of placing English credit at the highest standard in the civilised world.

CHAPTER XXVI.

BRANCH BANKING.

ONE of the distinctive features of modern banking is the establishment of branches throughout the country. This is shown in the tables prepared by Mr. James Dick for the paper read before the Bankers' Institute in April, 1892.

In 1883 there were 3932 offices, but in 1891 they had increased to 4934, or an average of seventeen offices for each bank.

Scotland has still a larger average of offices to the inhabitants than either England or Ireland.

For example:—

England . . .	1 to 8915 inhabitants.
Scotland . . .	1 to 4260 ,,
Ireland . . .	1 to 9520 ,,

For our guidance in considering the merits of branches, we cannot do better than remember the advice given to bankers by Mr. Rae in his excellent work, *The Country Banker*. He remarks that no bank ought to open a branch unless possibly for the following reasons, *viz.* :—

1st. It should be advantageous for the customers of that bank.

2nd. There should be a possibility of new business being obtained.

3rd. That the branch may act as a connecting link to other branches.

Branches should not be opened for the purpose of

competition with other banks, because that is not altogether desirable.

It must be remembered that when a bank is opened there is a tendency for the new institution to get all the bad or doubtful accounts.

Possibly the greatest use of branches is that they find an outlet for surplus capital. Thus if money cannot be employed to advantage at one branch, yet there might exist a demand for capital at another, and consequently none of the resources of the bank remain unemployed. If the surplus funds of a bank can always be utilised at a profit, it follows that a higher rate of interest can be given for deposits.

Mr. Gilbart, in his treatise on banking, says that for small towns a branch of a large bank is more advantageous than an independent joint-stock bank, because a branch can be worked at less cost.

There is no doubt that the establishment of branches by the existing banks of this country has been the means of preventing new institutions from starting. This would mean competition, which possibly might be advantageous to the community but detrimental to the existing banks.

In Scotland the branch system has been so extended that it would be almost impossible for a new bank to be formed. The Scotch banks have also the privilege of issuing notes, which enables them to provide till money at a trifling expense.

Competition between banks is not desirable, because greater risks and responsibilities are undertaken in order to secure profits.

Of course it is desirable that banking facilities should be provided at a small cost, but these facilities ought not to be at the expense of stability. If a branch is opened at a comparatively small cost, it enables the small trader and shopkeeper to keep banking accounts.

The vast increase in the country clearing in London shows that the branch system has been the means of inducing a fresh class of people to open banking accounts.

Mr. Barnett in 1881 estimated the country clearing at £350,000,000 per annum, and since that time there has been an enormous increase in the amount passed through the Clearing House. This shows that the branches have obtained quite a new connection. They have also been the means to some extent of superseding the country note circulation, because the cheque is now more utilised. Cheques which are received at the branches are sent to London daily, where they are cleared through the Clearing House.

It has also been stated that a bank with branches would be able to get the London Agent to transact its business at a lower cost than if the branches were separate institutions. This advantage is, however, not so important in the present day, because a large number of banks now have London offices. It is, however, advantageous for a bank to open branches in order to increase its connection, when by such means the new business obtained represents various industries, because a depression of trade would not then be so severely felt. In such a case branches would act as feeders, and give, as it were, new life to the central establishment. Again, if the customers of a bank have greater facilities given them, it is natural to suppose that they would recommend the bank to others.

Again, the branch system is the means of greater facilities for the transmission of money from one district to another.

Of course, the opening of new offices ought to increase the dividends to the shareholders, as banks naturally wish to increase their profits, if it can be done with safety. It seems, however, that the additional facilities

have to some extent benefited the customers rather than the banks.

The following figures show the dividends paid and number of branches after an interval of six years :—

Bank.	30th June, 1885.		30th June, 1891.	
	No. of Branches.	Dividend.	No. of Branches.	Dividend.
		%		%
Alliance	5	7	12	8
Capital and Counties	59	18	132	18
Central	7	10	11	10
City	8	10	12	11
Consolidated	4	10	9	10
Imperial	4	7	7	7
London and County	160	20	173	22
London Joint-Stock	6	12½	10	12½
London and Provincial	84	12½	119	15
London and Westminster	9	16	15	16
National	110	11	103	10
National Provincial	153	20	167	20
Union	5	12½	9	12½
London and South Western	53	6	91	8

From the above we notice that the banks which have increased their dividends are, with few exceptions, those which have opened branches in places where no banking accommodation previously existed; for example, the London and County, London and South Western, and London and Provincial, have opened branches in districts of greater London where no bank had hitherto been established. Although the fourteen banks have increased their deposits from £115,999,000 to £125,264,000, yet there has been no corresponding increase in the dividends. We must not, however, forget that in recent years there has been a steady decline in the rate of interest ruling in the market.

These banks, however, have increased their reserve fund from £8,035,000 to £8,839,000, which is very satisfactory, because it shows that they have provided additional funds to meet sudden emergencies.

Again, the additional reserve takes the place of increased capital, which is necessary when we consider that the liabilities have increased £10,000,000. Although some of the provincial banks have opened additional branches, yet their dividends do not show a corresponding increase. For example :—

Bank.	1881.		1891.	
	Branches.	Dividend.	Branches.	Dividend.
		%		%
Wilts and Dorset	64	22	83	22
Manchester and Liverpool .	54	20	50	20
North and South Wales . .	50	17½	65	15
Lloyd's Bank	43	20	130	17½

However, if the opening of branches has prevented other new banking institutions from starting, the result would be in time favourable to the existing establishments.

We will now consider some of the disadvantages which arise under the existing system of branch banking. It has been alleged that each office is in some sense a source of weakness, and this we believe is one of the reasons why the Bank of England has not opened more branches.

A recent writer in the *Economist* suggested that the Bank of England should have a large number of branches, like the Imperial Bank of Germany which has at present 250, but we must not forget that the Bank of England holds the cash reserve of this country. The existing banks would not like to see the Bank competing against them. The establishment of a branch means an additional responsibility to the directors; and it is impossible to suppose that they can understand thoroughly all the details and have a practical insight into the business of a town far away from the head office; they must to a great extent be guided by the manager of the branch, who supplies them with the necessary information. However,

the *real* responsibility for every branch must rest with the directors.

Again, any sudden demand for cash must be met from the central institution. The cash reserves of the banks have not, however, increased in proportion to the number of branches opened.

Mr. Goschen, in his celebrated speech at Leeds on 28th January, 1891, mentioned that eleven large banks kept in cash only 10·3 per cent. in 1888, whilst in 1879 they held 12·9 per cent. There does not appear to be any connection between the amount of cash held and the number of branches. The monthly returns issued by some of the banks show that some with the largest number of branches have the smallest cash reserve. No doubt if each branch was an independent bank, a larger cash reserve would be held. Of course, one must not forget that the facilities for the transmission of coin are greater now than they were fifty years ago.

It is also possible that if an issue of £1 notes takes place, as advocated by Mr. Goschen, it would be distinctly advantageous to a bank with a large number of branches. These notes could be sent to any branch at a trifling expense compared to the cost of transmitting gold. The National Banks in America keep $1 in cash for every $4 deposited. This gives a proportion of 25 per cent. in a country where branch banking is discouraged. A proportion of 10 per cent. to 14 per cent. of cash does not seem to be a sufficient reserve for banks which have a large number of branches.

We know that banks succeed because great confidence is placed in them, but if a branch happened to make a great loss it might cause a run upon all the branches. The bank might be perfectly solvent and yet be obliged to close its doors, because the head office might not be able

to supply till money to a large number of branches with sufficient rapidity.

It seems to us that a bank with a comparatively small number of branches is relatively stronger than one with a large number. The former would have, as it were, its business more concentrated, and consequently be able to supervise it more thoroughly. If a bank opens branches, it is a question whether that bank should not increase its capital. In America no new bank is allowed to be formed unless a certain amount of capital is assigned to it. The weakness of our system is that there has not been a corresponding increase of capital in proportion to the liabilities.

Mr. Gilbart stated some years ago that a bank's capital should not be less than one-third of its liabilities. No doubt this is a very high proportion, but it is questionable whether 10 per cent. is sufficient.

If we study the balance sheets of the Scotch banks we find that, although their deposits and branches have increased, their capital accounts remain stationary. Thus :—

	Capital.	Deposits.
	£	£
1865	9,431,000	56,185,000
1875	8,785,000	78,405,000
1881	9,052,000	78,283,000
1891	9,052,000	92,887,000

It must also be remembered that the Scotch banks have accepted the responsibilities of London institutions without increasing their capital account, but they have however increased their reserve fund to some extent. Quite recently it has been found necessary to reduce the rate of interest on deposits in consequence of the difficulty experienced in the employment of surplus funds. On the other hand, the rate of discount has been correspondingly lowered. The English banks have, however, increased their capital and reserve considerably. Thus to October,

1890, there was an increase in 12 months of £1,070,439 in capital and £869,088 in reserve.

The capital of the fourteen banks already mentioned amounts to £18,631,000, against deposits amounting to £125,264,000. This shows a greater proportion of capital for the English than for the Scotch banks.

Another disadvantage of branch banking is that there has been a tendency in recent years for banks to open branches in places where rival establishments exist. Possibly at such places there was enough business for one bank, but, with two, banking profits have been reduced to a minimum. There is no doubt that the opening of branches has been the means of extending banking facilities to a class who formerly did not avail themselves of them. We might say that fifty years ago no one opened an account with a bank unless he was able to keep a large balance. Banking in those days existed principally for the wealthy. In the present day any one can have a banking account, provided a small commission is paid.

The large increase in the deposits of the banks must be principally due to the fact that a new class have banking accounts.

We have already mentioned that the enormous increase in the country clearing in London is partly due to the increased banking facilities offered by the existing banks.

The following table shows the increase in the number of banking offices in various large towns, and we may presume that these branches would not remain open unless a profit was made:—

PROPORTION OF BANKS TO NUMBER OF INHABITANTS.

	1872.	1886.	1887.	1888.
Birmingham	31,000	15,000	11,000	10,000
Bradford	...	15,000	14,000	13,000
Leeds	25,000	28,000	22,000	20,000
Liverpool	29,000	12,000	11,000	11,000
Manchester	18,000	9,000	7,000	6,000
Sheffield	...	47,000	47,000	40,000

Between 1877 and 1889, banks were opened in 461 places where previously no bank existed. These great facilities for banking have been of much value to the community.

However, we must consider whether the present banking system is advantageous to all classes of society. The tendency of modern banking is one of amalgamation. New banks are not being formed for the purpose of providing additional facilities, which from time to time are necessary on account of growth of population and increased commerce. No doubt the public may benefit by these bank amalgamations in one way, *viz.*, by reducing the cost for banking accommodation. The working expenses of two banks which amalgamate ought to be less, especially if competition had previously existed between them.

On the other hand, it is not desirable to establish a monopoly of banking. We know that in Scotland it would be impossible for a new bank to start with any prospect of success. The branch system has been so extended in that country, combined with a monopoly of note issue, the *sine quâ non* of Scotch banking, that it would prevent a new institution from making a profit. It is possible that if the £90,000,000 of capital deposited in the Scotch banks were divided amongst twenty banks instead of ten, it would not be necessary for those institutions to compete with the London banks.

A system of monopoly might be the means of increasing the charges for banking facilities. It is, therefore, desirable to consider whether a monopoly of banking is being created in this country.

We think that the branch system is not desirable in one way, and that is the continual reference to the head office on all business of importance in connection with the

branch. We believe that in some banks no loans above a certain amount are allowed unless sanctioned by the head office. This not only means delay but it also makes the board of directors practically responsible for the business of every branch.

Again, it is not possible that directors can judge accurately upon a written report what is the real position of their customers. A *bonâ fide* applicant may not be able to get the accommodation he requires. We know that capital may be lent in some cases to persons without any risk, in fact without security, if a thorough knowledge of such persons is obtainable. A board of directors cannot possibly judge the *personal* character of customers who are unknown to them.

A bank may be transacting business in 150 different places where a diversity of trades and manufactures exists. It is questionable whether the wants of a local community are best satisfied by the branch system.

A recent writer in the *Economist* stated that the centralisation of control means the stifling of individual intelligence and energy, coupled with failure to gauge the needs of local commerce. It also meant the starving of enterprise in the provinces, because the capital of each district was sent to London for investment. No doubt the local wants of a community are best satisfied by a local bank, because if some new undertaking is required a local bank would be more inclined to assist than a board of directors in London. Of course a branch manager may be able to state accurately the requirements of the district to the board of directors, and thus satisfy the wants of the community. We think that a local bank with few branches, say for every county of England or spread over certain defined areas, would be the best system.

If a bank with a large number of branches failed, the distress occasioned by the failure would be felt over a larger area than if confined to one district. There is, of course, less possibility of capital lying idle in the case of a bank with branches over a large area, because, if not required for one district, it may be utilised in another. Banking, however, is now so much centralised in London that the metropolis has become the great distributer of capital. What we really want in banking is economy combined with efficiency. Our system must not only supply the wants of the community, but it must be perfectly sound. No breath of suspicion should ever reach any of our banking institutions. Every one admires and has an unlimited faith in the Bank of England, because it has always studied strength rather than dividends. It might have had branches throughout this country, but did not care to extend its responsibility, whilst it holds, as it were, the key of our banking system. We presume the Bank recognises that each branch established means in a sense additional responsibility, and also another outlet for specie payments.

We have already shown that the establishment of branches has not been, with few exceptions, the means of increased dividends. Some think that the high dividends paid by the banks should be the means of the public obtaining cheaper or better banking facilities.

On the other hand, it might be argued that facilities for banking are too cheap, because the banks of this country have at the present moment £39,000,000 of reserve on which no dividend is paid.

Possibly competition and the tendency for the rate of interest to decline have been the causes of stationary dividends. The profits made by banks on their total resources seem small. For example, the purely London

banks only earn 10s. 10d. per cent. on their total resources, but banks with country branches, where a higher rate is charged for loans, etc., earn from 15s. to 19s. 8d. per cent. Competition between banks is not desirable if it tends to speculation in order to maintain dividend, but, on the other hand, we do not want a monopoly of banking.

The remarks of Mr. Martin in the *Economic Journal* on "The Evolution of our Banking System" are well worthy of consideration. He says: "The provincial banks under the old system have done good service to the trade of this country. Intimately connected with the needs of their district, the position and character of their customers, they have fostered and developed local trade, agriculture and industries in a manner that might be impossible under new conditions. It has been made a complaint from Scotland that the resources of the country have, since the Scotch banks opened branches in London, been diverted from their legitimate use to the metropolis, and that heavy discount rates are charged locally, while the money is being employed at lower rates in the London money market. The same complaint has here and there been made in England, and it seems desirable that any change in the conditions of banking in this respect should take place gradually, rather than by any sudden movement that might entail some dislocation of local trade and industry."

There is a great difference between a bank which has gradually become larger and one which, in consequence of many amalgamations, has doubled its deposits.

It was recently stated by the official liquidator that one of the reasons why a certain bank failed was the difficulty of effective control and proper supervision over a branch so far away from the central establishment.

It is the age for large banking institutions, like it is the age for the conversion of large undertakings into limited companies. We can only hope that the great influence which large banks possess may prove beneficial to the community. If the banks satisfy the legitimate wants of the community, and charge a moderate amount for banking accommodation, there will be no justification in the remark that the tendency of modern banking is towards a monopoly.

One of the difficulties of the present day is that of the deposit system. We find reference made at bank meetings to the difficulty experienced in utilising deposit money. At times the rate for call money and three months' bills has been below the rate allowed on deposits, or the margin has been so small that no profit could be made, or not sufficient to pay working expenses. We do not think this ought to be the case, because the banks should be able to combine among themselves, and then either refuse deposit money or lower the rate so that a margin for profit should exist.

We have recently been reminded by the official liquidator that the high rate of interest allowed by a certain bank was one of the causes of its failure. At the present time we have a curious instance of the deposit system, and that is, the Government allowing £2 10s. per cent. on deposits which are invested in Consols realising £2 6s. 3d. per cent., in addition to the expenses of management, which amount to 9s. 1½d. per cent. Thus the total loss is about 13s. per cent.

During the present year Consols have risen to 112, and therefore the loss on the Savings Bank deposits is still greater. However, the present Chancellor of the Exchequer recognises the position, and will no doubt suggest some modification of the present system.

The deposits in the Savings Banks amount to £90,000,000 and in the Trustee Banks to £43,000,000. It seems an anomaly that such a loss should occur, and that the Government should compete for deposits against the other banks of the country.

Again, there is practically no cash reserve held against deposits amounting to £133,000,000.

CHAPTER XXVII.

BALANCE SHEETS.

THE study of the half-yearly or yearly statements issued by the banks is of great interest, because we have, as it were, reflected in them the policy of bank directors with regard to the management of the vast resources committed to their charge. One fact is apparent, and that is the absence of any fixed rule as to the proportion of capital, cash or investments that should be held against the liabilities. We give the following as a good illustration of a balance sheet :—

LIABILITIES.	ASSETS.
Current accounts . . .	Cash in hand and at Bank of England . . .
Deposit accounts . . .	Money at call and short notice . . . .
Other liabilities, circular notes, letters of credit, etc. . .	Investments . . .
Acceptances	Consols . . . .
Capital paid up . . .	British Colonial Government Corporation Stocks
Reserve fund	Other securities . . .
Rebate on bills not due . .	Bills discounted—
Profit and loss . . .	(a) three months and under
Balance brought forward .	(b) exceeding three months
Net profit for the half-year .	Loans and advances . .
	Liabilities of customers for acceptances . . .
	Bank freehold and leasehold premises, furniture and fittings . . . .
	Other assets . . .

PROFIT AND LOSS ACCOUNT.

Interest accrued and paid .	Balance brought from last account . . . . .
Current expenses . . .	Gross profits for the half-year after providing for bad and doubtful debts.
Salaries, rent at head office and branches . . .	
Rebate on bills not due . .	
Dividend.	
Bank premises account . .	
Balance carried forward. .	

In our analysis we will first consider the liabilities, which consist of capital, reserve, deposits, acceptances, and sundry other items. The capital represents the amount which is thought sufficient to carry on the business of banking. The reserve is the accumulation of undivided profits, and the proportion of these two items in the case of London banks varies from 7 per cent. to 29 per cent. of the liabilities. Acceptances represent bills accepted for correspondents, and which must be paid by the banks when they mature. Lastly we have the current and deposit accounts; it would be desirable if the former accounts were separated from the latter, which represent a different form of liability. Deposits may be called in at any moment, and the depositor has not the same interest in the bank which the customer possesses. When there is a feeling of distrust in the financial world, the depositor is the first to withdraw his capital.

The assets should be carefully examined, because the stability of our banking institutions is largely dependent upon the investment of the great resources committed to their charge. The first item would be the cash reserve of the bank, which consists of cash in hand, at the Bank of England, and money at call.

We can scarcely consider money at call as a cash reserve, because during a crisis it would be almost impossible to call in money from the brokers.

It is worthy of notice that some banks do not group their cash with money at call, but include such amounts with their advances.

The proportion of cash would vary from 7 to 20 per cent.

The average of seventeen London banks is 14·5 per cent., and of money at call 12·7 per cent.

The next item in the balance sheet is the investments, which are of a varied character. At the head of the list would be Consols, which form the best security, because the payment of interest is secured on the revenues of the country and the stock can always be converted into cash at short notice.

Some banks invest the whole of their capital or reserve in Consols.

The next class of investments would be Indian Government Stocks, Colonial Government Stocks, Corporation Stocks and English Railway Debenture Stocks.

These items would vary from 9 per cent. to 36 per cent., the average of seventeen London banks being 25·5. It is satisfactory to note that the private banks which have published balance sheets show a very high proportion of English Government Stocks. Unfortunately for the banks, the yield of interest every year tends to get less.

For example, the yield from Consols is about £2 6s., and from Colonial Government Stocks about £3 5s. The various classes of investments should be separated in order to get a correct opinion as to the bank's position. The proportion of cash, money at call, and investments to current and deposit account varies from 39 to 63 per cent. in the case of the London banks.

The most important item in the balance sheet is loans and advances to customers, and also bills discounted. Some banks separate the bills discounted from the advances, which it is thought should be done in all cases. Of the two classes, *viz.*, bills and advances, bills would stand first, because they form a better security. As a rule bills are met at maturity, but it sometimes happens that loans are not repaid when they fall due.

A banker must concentrate his attention upon this important item in the balance sheet, because public

confidence in the management is largely dependent upon loans and advances being made with great discretion.

The acceptances are shown on each side of the balance sheet, and vary considerably from 1 per cent. to 38 per cent. against the total amount of deposits.

We have already considered whether it is advisable to extend this class of business.

The last item in the balance sheet is bank premises, the usual custom being to reduce the amount gradually.

With regard to the profit and loss account, it is simply a statement showing how it is proposed to divide the net gains made during the half-year.

The profits of a bank are, of course, dependent upon the interest obtained by lending, as it were, the assets. The cash reserves of the banks form a contingent fund, and, therefore, we might say that about 14 per cent. of the assets do not produce any income. In recent years the tendency is for investments to increase and loans and advances to decrease. This naturally means less profits, because the rate of interest on all first-class investments is being reduced.

The monthly balance sheets and half-yearly balance sheets are now keenly criticised, and this we think will in course of time tend to strengthen our banking system.

We have seen that great changes have taken place in our banking system from an early period, and especially during the present century. This change is still going on; many banks after a long and honourable career are being merged into large banking institutions.

At present it is difficult to form an opinion with regard

to the new system, but if in the future banking in this country is to be transacted by a comparatively small number of banks, it is highly desirable that adequate cash reserves should be held, and also that a perfect system of audit be adopted.

Another subject may be mentioned in connection with banking of the present day, and that is bimetallism. Any change in our system of currency may have a very important effect upon banking and commerce, and therefore the subject of bimetallism should be understood in order to ascertain how far the trade of this country would be affected by any such alteration. We have recently seen a rich country like the United States compelled to protect its gold reserves, in consequence of unwise silver legislation in former years. Again, we notice public opinion in Germany being in favour of bimetallism, and therefore it is important for England, if necessary, to uphold her present system of currency. We do not intend to state the arguments for and against bimetallism, but wish to point out how deeply such changes may affect our banking system.

The formation of the Institute of Bankers in 1879 has been of great service to banking, because it has endeavoured to promote uniformity of practice amongst the banking institutions of this country.

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